S. HRG. 107–229

AGRICULTURE MARKET CONCENTRATION

HEARING

BEFORE A

SUBCOMMITTEE OF THE

COMMITTEE ON APPROPRIATIONS

UNITED STATES SENATE

ONE HUNDRED SEVENTH CONGRESS

FIRST SESSION

SPECIAL HEARING

MAY 17, 2001—WASHINGTON, DC

Printed for the use of the Committee on Appropriations

Available via the World Wide Web: http://www.access.gpo.gov/congress/senate

U.S. GOVERNMENT PRINTING OFFICE

76–970 PDF WASHINGTON : 2002

For sale by the Superintendent of Documents, U.S. Government Printing Office
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AGRICULTURE MARKET CONCENTRATION

THURSDAY, MAY 17, 2001

U.S. SENATE,
SUBCOMMITTEE ON AGRICULTURE, RURAL DEVELOPMENT, AND RELATED AGENCIES,
COMMITTEE ON APPROPRIATIONS,
Washington, DC.

The subcommittee met at 10 a.m., in room SD–138, Dirksen Senate Office Building, Hon. Thad Cochran (chairman) presiding.

Present: Senators Cochran, Specter, Kohl, Durbin, Dorgan, and Johnson.

OPENING STATEMENT OF SENATOR THAD COCHRAN

Senator COCHRAN. Please come to order. It's a pleasure to convene this morning a hearing of this subcommittee, the Subcommittee on Appropriations for Agriculture Rural Development and related agencies.

We meet today to consider the issue of market concentration in agriculture and the effect it may have on the funding of programs under the jurisdiction of this subcommittee.

In 1996, the Department of Agriculture formed an advisory committee to investigate concentration in the agricultural economy, and over the past several years, funds have been appropriated to implement the advisory committees' recommendations.

Among these recommendations were increased monitoring and enforcement of antitrust and regulatory policy, advising producers about requirements to obtain a contract, and action to end inequities in meat inspection.

The advisory committee also recommended mandatory livestock price reporting which was included in the fiscal year 2000 funding bill for the Department of Agriculture, and it implemented by the department last month.

The debate over concentration and consolidation in agriculture and the appropriate role of the Federal Government in regulating markets and whether changes in current laws would be appropriate will be issues for consideration during the reauthorization of the farm bill.

We hope to learn more about these issues today, including the consequences of activities we have funded in the past and which have been implemented.

We're pleased to have with us three panels of witnesses whose statements will be made a part of the record in full.

In the first panel, we're pleased to welcome Keith Collins who is Chief Economist with the United States Department of Agriculture.

JoAnn Waterfield, Deputy Administrator of the Packers and Stockyards Programs of the Department of Agriculture. And John M. Nannes, who is Acting Assistant Attorney General with the Antitrust Division of the Department of Justice.

Before proceeding to hear from our witnesses, I'm going to yield at this point to other senators on the subcommittee for any comments or opening remarks they would like to make.

My distinguished friend from Wisconsin is the ranking member on the committee, Senator Kohl.

STATEMENT OF SENATOR HERB KOHL

Senator KOHL. I thank you very much, Mr. Chairman. Mr. Chairman, if there has been one single rallying cry over the years, it is to support the Federal Farm Programs. It would be a statement of determination to save the family farm. That proclamation has been a constant theme in the halls of Congress and throughout the countryside.

This phrase often conjures up the vision of the small scale, fiercely independent operator modeled after the principle of the yeoman operator that Thomas Jefferson considered to be the basic ingredient of American democracy.

So we might ask what are we to save the farm from? One obvious answer is to save it from the grip of unwarranted market concentration.

Aside from our basic ideals of government, the United States has perhaps no better demonstration of genius than our economic system. The free flow of goods and services throughout our country and our general principles of commerce have established the most powerful economic force in the world.

The simple concepts of supply and demand do, in fact, work. Our responsibility is to assure that conditions of law, policy, and economics in which supply and demand thrive are always present. And so our focus today is to examine the extent to which market concentration threatens this delicate balance of economic forces.

The panels assembled here today will provide a broad range of information necessary to better understand just what is at stake in this debate and the form in which the debate should be drawn.

I especially want to recognize Professor Peter Carstensen of the University of Wisconsin School of Law for his special expertise and long work on these issues, and for his previous assistance when we examined some of these issues before the judiciary subcommittee on antitrust business rights and competition, on which I am also the ranking member.

So I look forward, along with the rest of this panel, to today's discussion and also to hearing suggestions on how this subcommittee might better work to support a sound agricultural economy. Thank you, Mr. Chairman.

Senator COCHRAN. Senator Johnson.

STATEMENT OF SENATOR TIM JOHNSON

Senator JOHNSON. Thank you, Mr. Chairman, for holding what I think is a very timely and very important hearing. Anticompetitive concentration issues are a matter of great concern and impor-

tance all across farm and ranch country in America today and certainly in my home State of South Dakota.

Over 60 rural groups recently wrote the House Ag Committee seeking the first time inclusion of a competition title in the next farm bill, a request that I enthusiastically support, of which I think is a reflection about the broad-based concern about the underlying structure of American agriculture and the direction that we are going today.

This is not the Ag Committee, obviously. This is the Agriculture Appropriations Subcommittee, and our issues are a bit narrower but nonetheless critically important on this subcommittee.

I'm concerned, Mr. Chairman, that USDA's marketing regulatory operations budget has been slashed by $231 million in fiscal 2001, and that the Ag Marketing Service has been cut from $61 million in that fiscal year, a cut that I fear may not permit the AMS to successfully administer our new mandatory price reporting program, one of the key strategies that was put in place just this past year in the hopes of leveling the playing field, so to speak, between independent livestock producers and the packing industry.

Moreover, the Grain Inspection Packers and Stockers Administration or GIPSA budget has been essentially flat lined, and I fear that that may not equip them to investigate and guard against unfair trade practices in the packing industry.

Last year the GAO reported that GIPSA lacks the staff, budget, and expertise to properly investigate anti-competitive behavior in livestock markets. That was prior to taking on a flat-line budget this year.

GAO recommended the GIPSA require an earlier integration of attorneys in the planning and review of investigation and closer consultation take place between GIPSA, the Department of Justice, and FTC during investigations. And I look forward to learning how GIPSA plans to meet these recommendations under their tight budget constraints.

Farmers and ranchers have weathered a storm of mergers in recent years between grain producers, seed and biotech companies, railroads, equipment dealers, grocery chains, meat packers. This is a matter of utmost importance.

Our farmers and ranchers, I think, understand that the open marketplace is still the major price discovery mechanism that independent producers must rely on to gain a fair price. But when the open market is then lacking in activity, the ability of one or two players to affect that market is enormous.

PREPARED STATEMENT

So I look forward to the testimony today. I welcome very able panels that the chairman has invited to share some insights with us today, and I look forward to this hearing.

Senator COCHRAN. Thank you, Senator.

Senator JOHNSON. I have a formal statement to offer.

Senator COCHRAN. That will be included in the record.

[The statement follows:]

PREPARED STATEMENT OF SENATOR TIM JOHNSON

Thank you Chairman Cochran for holding this subcommittee hearing on marketplace concentration in agriculture. Without a doubt, concentration in agriculture is one of the most serious issues facing family farmers and ranchers today. I believe Congress and the Administration must always promote and protect real competition as a key element of our free enterprise economy—the envy of the capitalistic world—so I thank Chairman Cochran and Senator Kohl for conducting our hearing.

I believe that if Congress and the Administration fail to cooperate to restore competition in all commodity and livestock markets now, the results will be crushing for independent family producers and the entire fabric of rural America. Agricultural producers want to derive income from the marketplace, but in order to assure that can happen, Congress must act now to restore fair competition to crop and livestock markets.

Given that farm income is in-part dependent upon competitive commodity and livestock markets, over 60 farm and rural groups recently wrote the House Agriculture Committee seeking the first-time inclusion of a "competition title" in the next farm bill, a request I enthusiastically support. It is clear by this recent appeal and the number of witnesses present to testify on this subject today, that competition policy is extremely important to the overall prosperity or decline of rural America.

Regarding USDA's budget proposal for fiscal year 2002, I appreciate the President's desire to fund national priorities in a restrained way so as to provide significant tax relief to America's working families. I too support a significant tax cut. Yet, we must address the budget and tax cut in a balanced fashion, assuring efforts are made to pay down the Federal debt and fund key programs—such as USDA efforts to promote competition in agriculture. While USDA's proposed budget adequately addresses some of our priorities, I believe it fails to make some specific and significant investments in a secure farm safety net, conservation programs, and efforts to restore marketplace competition.

For instance, the Agricultural Marketing Service (AMS) budget has been cut by $61 million from fiscal year 2001. The mission of AMS is to promote competitive and efficient markets, and AMS must carry out the bulk of our new mandatory price reporting program. I am concerned a cut in the AMS budget may not permit the successful and complete administration of mandatory price reporting.

Moreover, the overall Marketing and Regulatory Programs budget has been slashed $231 million from fiscal year 2001, the Grain Inspection, Packers and Stockyards Administration (GIPSA) budget has been essentially flat-lined, and I do not have confidence that GIPSA's budget adequately equip that agency to investigate and guard against the unfair trade practices by meatpackers. This is very troubling because a September 2000 General Accounting Office (GAO) Report asserted that GIPSA lacks the staff, budget, and expertise to investigate anti-competitive behavior in livestock markets. Therefore, GAO recommended that GIPSA require an earlier integration of attorneys in the planning and review of investigations and closer consultation take place between GIPSA, the Department of Justice, and the Federal Trade Commission during investigations. Last year, Congress concurred and required GIPSA to implement GAO's recommended improvements by the passage of the Grain Standard and Warehouse Improvement Act of 2000 (Public Law 106–472). I look forward to learning how GIPSA plans to meet the mandate of Congress on this matter.

Overall, it seems to me we need more competition in agriculture, not less. However, the proposed wave of mergers and acquisitions among agribusinesses has set the stage for anticompetititve agriculture. Farmers and ranchers have weathered a storm of mergers in recent years between grain processing giants, seed and biotechnology companies, railroads, farm equipment dealers, retail grocery chains, and meatpackers. Now that Tyson Foods has turned its back on the acquisition of IBP, it's not clear if the meat giant's two other former bidders remain interested. While many analysts suggest that IBP's competitors are not now interested in a deal, the stage is still set for concentration to sweep competition away, leaving independent farmers and ranchers without an active marketplace in which to sell their crops or livestock.

On a broad scale, concentration in agriculture results in a marketplace with a small number of firms controlling transactions of agricultural goods between producers and consumers—and these firms leverage a dominating amount of bargaining power over both producers and consumers. On a specific scale, consider the meatpacking industry. Prior to 1990, horizontal concentration by meatpackers swept the nation, leaving the U.S. with three or four big meatpackers left to purchase beef cattle, pork, and lamb for slaughter. After 1990, these same firms added the ele-

ment of vertical integration to their arsenal, effectively controlling much of their slaughter needs through captive supply and outright livestock ownership. The consequence for independent producers was a meager cash marketplace without much competition among meatpackers at all.

Yet, that open marketplace is still the major price discovery mechanism that independent producers rely upon to gain a fair price. So, when the open market is thin and lacking activity, the ability of one or two dominant meatpackers to affect the market is tremendous. For instance, if in a given week a meatpacker utilizes all of its captive supplies and packer owned livestock to fill its kill needs, it has the ability to level off a price spike or even depress prices paid in the open market. Despite a producer's best effort to raise a quality live animal, the power leveraged by a packer or group of packers can destroy the opportunity to ensure a fair price.

A USDA–GIPSA study of cattle procurement practices by meatpackers in the Texas panhandle region of the U.S. found a "robust correlation" between higher captive supplies (and packer ownership) and lower spot cattle prices "in every case." Captive supplies are livestock generally controlled by packers through outright ownership or contractual agreements. This indicates to me that when meatpackers own large percentages of their slaughter requirements, the volume and vigor of a cash or open market is significantly reduced.

According to Dr. Ron Plain, agricultural economist at the University of Missouri, 75 percent of hogs are either packer-owned or under production contracts by packers. Other studies and estimates indicate at least nearly 60 percent of the slaughter market for hogs is under packer ownership and control while some economists predict the open market for live hogs will disappear in five years.

In beef cattle slaughter, meatpacker industry figures show that on average about 5 percent of slaughter is actually packer owned. Yet, because USDA seems unable to determine the exact level of captive supply controlled by packers through contracts and other marketing arrangements, this figure could be misleading. Additionally, due to a small number of beef packers controlling around 80 percent of overall slaughter, some regions of the country have one packer feeding and owning around 14 percent of its slaughter needs. According to USDA–GIPSA, overall captive supply, on average, is nearly 20 percent of total fed beef slaughter.

Independent cattle feeders and farmers used to have several buyers competing for their cattle every day of the week. With increasing captive supplies, packers do not bid aggressively for cattle to fill their slaughtering needs. In some instances, cattle feeders have only a few hours within one or two days a week to accept packer bids for cattle, most often in "take-it-or-leave-it" scenarios. Economists consulting the Western Organization of Resource Councils found that for each percent of captive supply, spot or cash prices decreased by eight cents per hundred weight.

A decision on the part of one meatpacker may have a substantial effect on the marketplace. For example, when Smithfield shut down the pork plant in Huron, South Dakota—formerly owned by American Foods Group—pork producers in my State were left with merely a single market for their slaughter hogs. Alternatively, a decision on the part of a livestock producer seller has little if any effect at all on price. What does this mean? It means the marketplace is not competitive.

It is now evident that current meatpacker livestock procurement practices (packer ownership, captive supplies, and other marketing arrangements) tend to transpire outside the open, cash, spot market. As a result, the process of bidding in an open fashion for the purpose of procuring slaughter livestock—which is really central to competition and a cornerstone to free-enterprise—is fading away. Therefore, livestock producers—who depend upon competitive bidding to gain a fair price—are forced to either enter into contractual, ownership, or marketing arrangements with a packer or find themselves squeezed out of marketing opportunities.

I have introduced bipartisan legislation to restore a competitive bidding process to slaughter livestock markets, and in turn, ensure the future economic security of independent livestock producers. I have been joined by Senators Grassley (R-IA), Thomas (R-WY), and Daschle (D-SD) in introducing S. 142 (the RANCHER Act) to prohibit meatpackers from owning livestock prior to slaughter.

This legislation has the support of the National Farmers Union, the South Dakota Farmers Union, the South Dakota Cattlemens Association, the Center for Rural Affairs, the Organization for Competitive Markets, Ranchers—Cattlemen Action Legal Fund (R–CALF), the Iowa Pork Producers Association, and Illinois Farm Bureau Federation.

My legislation is timely because of recent movement in the meatpacking industry (Tyson's failed effort to buy IBP, Smithfield's uncertain plans with IBP) to choke-off market access from independent livestock producers. My bill recognizes the need for greater value-added opportunities and exempts producer owned and controlled cooperatives and small producer owned meatpackers from the ownership prohibi-

tion. This legislation is also retroactive, requiring meatpackers to divest of ownership interests in slaughter livestock.

Despite the alleged criticism, a ban on packer ownership of livestock would not drive packers out of business. As indicated in earnings reports and press releases from the major packers, most of their income and earnings are generated from branded products and companies marketing products in a more direct fashion to consumers. My bill would not limit IBP, Conagra, Cargill, or Smithfield from buying food service companies, branding foods, or finding new global markets. The bill simply forbids meatpackers from owning livestock prior to slaughter.

It should also be noted that other industries in America have limits on vertical integration. For example, network broadcasters are limited in their ability to own local television and radio stations. Similarly, movie production companies are not allowed to own movie theaters. Finally, Barnes and Noble—the nation's largest bookseller—was recently prevented from buying out the nation's largest book distributer.

For many years, those who support captive supplies and vertical integration have held contract poultry production up as a role model for where to go with pork, beef, and lamb. Under their model, farmers make significant investments in sole-purpose buildings using their own capital, and sign contracts with large, integrated companies. The contractual terms stipulate that the farmer provides the labor, management, and facilities required to raise the company-owned birds to the appropriate slaughter weight. Unfortunately, due to a lack of bargaining power on the part of poultry growers, the typical contract relationship between growers and the poultry companies has become more and more one-sided, leaving many producers with "take-it-or-leave-it" contracts with very unfavorable terms. The companies control all the production decisions, leaving the growers little if any independence in the decision making process on their own farms.

Unfortunately, the poultry model is now being emulated by the processors of other livestock and commodities. According to GIPSA, "the percentage of hogs produced through various production and marketing contracts has increased sharply in recent years, and now accounts for 65 percent of all slaughter hogs." For the 2000 season, all the major tobacco companies are now contracting with growers for some portion of their domestic supplies. Other commodities commonly produced under contract include, but are not limited to: beef cattle, corn, soybeans, sugar cane, and cotton. Without the establishment of basic farmer or rancher safeguards, many of the producers of these commodities potentially face the same pattern of abuse experienced by poultry growers.

It all boils down to whether we want independent producers in agriculture, or if we will yield to concentration and see farmers and ranchers become low wage employees on their own land. I'm proud to stand up for competitive agriculture that boasts a broad base of independent, family farmers and ranchers. I look forward to the insight that today's witnesses will provide to our discussion of agriculture concentration. Thank you Mr. Chairman, this concludes my opening statement.

Senator COCHRAN. Mr. Collins, we'll begin with you. We appreciate your attendance and furnishing us with a prepared statement. It will be made a part of the record in full, and we ask you make whatever summary statements you should choose.

STATEMENT OF KEITH COLLINS, CHIEF ECONOMIST, DEPARTMENT OF AGRICULTURE

Mr. COLLINS. Thank you, Mr. Chairman, Mr. Kohl. Mr. Johnson. Thanks for the invitation to participate in this hearing today. I'm going to comment as an overview to start your day on forces driving consolidation in food and agriculture and some of the economic issues that these trends have raised.

Consolidation and concentration in the food system refers to changes in number, in the size distribution of firms and agribusiness firms as well as changes in the business arrangements they make among one another.

A primary cause is economies of scale, which allows larger volumes to be produced and marketed at lower per unit cost, and usually that's due to more efficient production plants or managing systems or distribution methods.

Consolidation can also be caused by other factors. Economies of size, for example, can provide, increased access to capital for research and advertising, volume-based price reductions on production inputs that a large firm can buy or premium price on large volumes of specific outputs they might be able to sell.

Still other factors that can generate concentration and consolidation include the exit of firms from an industry due to inability to compete or the desire to seek higher returns in a different industry. The ability to serve larger markets may also contribute to merger activity as firms try to build on distribution networks of already established smaller firms.

STRUCTURAL CHANGE

An important aspect of structural change is increased coordination in the farm to consumer chain, which refers to contractual arrangements, alliances, joint ventures, or vertical integration.

Consumers in America today are increasingly demanding higher quality food products that offer nutritional benefits, convenience, freshness, and taste. Contraction and vertical integration help downstream firms ensure that they can provide such characteristics, and that they are provided when they're needed and with minimal inventory costs.

With these as driving forces, there has been substantial consolidation and the emergence of large firms in a variety of markets tied to farming, from input suppliers to retail grocers.

For example, while we still have thousands of farm machinery dealers today, very few companies produce tractors or large equipment. Much of that consolidation occurred a long time ago so that by 1986 the top four tractor firms had 80 percent of the market.

The more recent example of rising consolidation is in the seed industry where major restructuring took place in the 1990s. Large chemical or pharmaceutical companies acquired seed businesses as a way to complement their existing agricultural chemical businesses and their expertise in molecular biology. One study placed the four firm concentration ratio in 1998 at 67 percent for corn seed sales, 49 percent for soybean seed sales, and 87 percent for cotton seed sales.

At the other end of the food chain, the market share of the largest 20 food retailers increased from 39 percent to 52 percent during the 1990s. Analysis of the 100 largest U.S. cities found that the market share of the four largest food retailers was 72 percent in 1998. Although that was up very little during the 1990s.

Consolidation has also occurred between the farm input industry and the food retail markets. In farm production it has been occurring for decades. And recently it has been very rapid for hogs and milk production. It's also occurred in grain handling and transportation, particularly among railroads and barge lines.

It's occurred in much of the food processing sector such as meat packing, especially for cattle slaughter during the mid 1980s and hog slaughter during the 1990s.

The economic growth in a market-oriented economy like the one we live in involves business formation, internal expansion, mergers, acquisitions, and alliances of various kinds. It also includes spinoffs, divestitures, and exits. These dynamics of change have

generally resulted in consumer products being more efficiently produced and of higher quality and lower price than otherwise.

Nevertheless, there are a number of concerns that bear our attention. One issue is the extent to which increasing concentration increases the ability of firms to exercise market power. The firms with market power may successively mark up prices charged to consumers or depress prices paid to farmers below competitive levels.

They may also shift costs to farmers by demanding certain services. Increasing concentration may also facilitate collusion or other relationships between firms that inhibit competition. These issues need to be examined in well-defined markets and with careful attention to the possible actions of existing competitors which could include producers of substitute products and the potential for entry of new competitors.

A second issue is the extent to which increasing concentration reduces product innovation and development.

A third issue is the extent to which increasing competition affects the ability of sellers, such as farmers, to find markets for their products as vertical integration thins out some markets.

A fourth issue is market transparency and the need for access to adequate, timely information on market conditions to avoid putting firms at a competitive disadvantage.

As food and agricultural markets have moved from being local markets to regional markets to national markets to global markets, businesses in the food system have moved towards larger scale of production. While this evolution can improve coordination within the food chain and the response to changing consumer preferences, the potential for market power increases. This makes monitoring of markets, provision of information and enforcement of the antitrust laws increasingly important to farmers and consumers.

PREPARED STATEMENT

These are responsibilities that the Justice Department is very concerned with, and these are responsibilities that we take very seriously at USDA. And Ms. Waterfield will describe some of our actions in that arena. Thank you, Mr. Chairman.

[The statement follows:]

PREPARED STATEMENT OF KEITH COLLINS

Mr. Chairman and members of the Subcommittee, thank you for the invitation to participate in this hearing to discuss concentration in the U.S. food system. All segments of the agricultural sector are undergoing structural change for a wide variety of reasons. I will examine some of the factors contributing to consolidation and concentration in the food production and marketing system and briefly present data on recent structural trends in the food system, including farm inputs, farm production, transportation, processing, merchandising, and retailing. Lastly, I will discuss some of the economic issues that have been raised regarding increasing levels of concentration in the food production and marketing system.

The U.S. food and fiber system, which includes farming and related industries, accounted for 16 percent of U.S. gross domestic product (GDP) in 1999 and employed over 24 million people, or 17 percent of the U.S. labor force. Although farming employs only about 1 percent of the U.S. workforce and accounts for less than 1 percent of total GDP, the contribution of farming to the national economy is much greater because of production agriculture's reliance on other industries for production inputs and for the processing, merchandising, and retailing of the products farmers and ranchers produce. The efficiency of this system has enabled U.S. agri-

culture to provide an abundant, safe and affordable food supply for U.S. citizens and to be a dominant supplier of food and fiber to the rest of the world's population.

REASONS FOR CONSOLIDATION AND CONCENTRATION

Consolidation and concentration in the food system refers to changes in the number and size distribution of farms and agribusiness firms and the changing business arrangements farms and firms make with one another. Structural change is studied because of concerns over the economic and social effects of certain business structures, particularly consolidation of farms and firms. Consolidation of firms into very large production units is sometimes called "industrialization."

Many factors contribute to consolidation and concentration in the U.S. food system. A primary cause is economies of scale. Economies of scale allow larger volumes to be produced at lower per unit production costs, thereby increasing a firm's potential profitability. These economies can take many forms, such as larger and more automated production and processing facilities, reduced overhead costs, and lower distribution costs. Consolidation may also be encouraged by pecuniary economies related to size, such as increased access to capital for research and advertising, volume-based price reductions on production inputs which can lower per unit production costs, or premium prices on large volumes of specific outputs which increase per unit returns. Other factors that can generate consolidation include the exit of firms due to the inability to compete with more efficient firms, the decision of entrepreneurs and providers of capital to seek more lucrative business opportunities in other industries, and government programs, including farm programs, tax provisions, research programs and credit programs. The emerging global economy may contribute to merger activity, as firms try to build on the distribution networks already established by smaller firms operating within countries.

Some have suggested that the slow overall rate of growth in food consumption also contributes to structural change. Slow growth in food consumption may cause firms to look for a competitive edge by offering new products and to expand long-term growth and profitability by increasing and diversifying their product lines through mergers and acquisitions.

An important aspect of structural change is increased "coordination" in the farm-to-consumer chain, which refers to contractual arrangements, alliances, or vertical integration. Consumers are increasingly demanding higher quality food products that offer nutritional benefits, convenience, and taste, rather than simply bulk or homogenous commodities purchased for home meal preparation. Contracting and vertical integration help downstream firms ensure that the commodities produced by farmers and ranchers and processed into food products meet the specific characteristics consumers want and that those products can be provided as needed with minimal inventory costs.

RECENT TRENDS IN CONCENTRATION

Farm Inputs: Farm Machinery.—In 1997, 1,263 establishments produced farm machinery in the United States, delivering nearly $16 billion in products. That compares with 1,576 companies that delivered about $7 billion in products 10 years earlier. The industry consists of a small number of full-line manufacturers that produce complete lines of equipment, including tractors, combines, tillage, and planting equipment, and a large number of smaller firms producing specialized equipment for regional markets. The industry has undergone substantial consolidation for many decades, especially for producers of large equipment, such as tractors. As farming transitioned from horse to machine, numerous tractor manufacturers emerged. The fate of most of these firms paralleled the consolidation in the auto industry with many brand names disappearing as the century unfolded. A significant industry shakeout occurred during the farm credit crisis of the 1980's when farmers sharply reduced farm machinery purchases, leading to a series of mergers, acquisitions, and joint ventures in the industry. By 1986, the top four firms accounted for 80 percent of tractor sales. While no data are available on the current four-firm concentration ratio-the percentage of market share controlled by the four largest firms-tractor sales continue to be dominated by a few firms.

The number of farm machinery dealers also declined sharply as the number of major manufacturers declined, inventory costs increased, and small dealers could not the afford parts and service departments that larger competitors could provide. In 1997, there were 6,937 farm machinery dealers selling primarily to farmers, but many of these were owned or franchised dealerships of manufacturing firms.

Farm Inputs: Seeds.—A major restructuring took place in the seed industry during the 1990s as large, multinational agricultural businesses purchased or formed joint ventures with smaller seed and plant breeding companies. Many of the large

companies were chemical or pharmaceutical companies, so acquiring seed businesses appears driven by an effort to complement their existing agricultural chemical businesses and their expertise in molecular biology. The pace of consolidation was rapid and significant in scope. One review of consolidation activity for 1998 found that 10 biotechnology firms were involved in 186 mergers, acquisitions, joint ventures or other collaborations or alliances. A 1999 study by Iowa State University placed the four-firm concentration ratio in 1998 at 67 percent for corn seed, 49 percent for soybean seed, and 87 percent for cotton seed.

During 2000 and 2001, some of these multinational companies spun off or announced plans to sell agricultural divisions. These decisions may reflect ongoing difficulties in the biotech seed industry, such as some consumer resistance, or higher-than-expected development and commercialization costs. Nevertheless, the restructurings that occur are likely to continue to leave the seed industry dominated by a few large players.

Farm production.—Rapid consolidation occurred in farm production between 1935 and 1970, as the number of U.S. farms fell by over 50 percent, from 6.8 million to under 3 million. The primary factor contributing to the decline has been increasing mechanization. Mechanical power, larger, more efficient farm equipment, and improvements in farming methods greatly increased labor productivity in agriculture after the mid-1930's. Because of increasing productivity, less labor was needed to produce crops and livestock, allowing farmers to expand the size of their operations. In addition, technological advances in livestock, poultry, and milk production enabled large numbers of animals to be managed in confined operations. Increasing productivity tended to keep returns low especially for those producers who failed to adopt cost-cutting technologies, contributing to the decline in farm numbers. Despite the rapid consolidation in farm numbers, over 90 percent of farms remain family operated.

Over the past decade, farm numbers have stabilized as many farm households have been able to supplement their farm income with income from off-farm jobs. In 1935, the incomes of farm-operator households averaged 40 percent below the average income of non-farm families. In recent years, the average income of farm-operator households has exceeded the average income of non-farm families. In 1999, the income of non-farm families averaged $55,000. The Economic Research Service (ERS) estimates the total income of farm-operator households averaged $64,000 in 1999, with about 90 percent of the income coming from off-farm sources. While farm numbers have declined over time and a larger share of production is accounted for by an increasingly smaller number of producers, production remains largely unconcentrated for major crops. According to the Census of Agriculture, there were 359,666 farms growing corn for grain; 241,334 farms growing wheat for grain; and 353,566 farms growing soybeans in 1997.

There were 1.011 million farm operations with cattle in 1997. The pace of concentration for cow-calf operations has remained well below that of other livestock and poultry sectors. However, of the approximately 110,000 feedlots in 1997, the largest 2 percent marketed 85 percent of the fed cattle. The four largest feeding firms had annual feeding capacity in 2000 equal to 11 percent of total annual steer and heifer slaughter. In 1997, there were 99,238 dairy, 63,246 poultry, and 102,108 hog farms. In 1997, 3 percent of hog farms accounted for over 50 percent of sales and 3 percent of dairy farms accounted for over one-third of milk sales. Poultry production was less concentrated but 95 percent of the broilers are produced under contract to fewer than 40 firms. While consolidation in hog and poultry production appears to have slowed, the movement to larger and fewer dairy operations continues.

Handling and transportation.—Based on data from the Grain Inspection, Packers and Stockyards Administration, market shares of the four largest agricultural export firms ranged from 47 percent for wheat to almost 70 percent for corn in 1998. While the share of total U.S. wheat exports held by the four top firms has remained relatively constant over time, the U.S. corn export market has become more concentrated. The export share for soybeans of the four top firms declined over the period from 1985–98. The changes in aggregate U.S. market share may mask changes at a particular port and the fact that the four top companies for some markets may have changed from period to period. In general, those reporting areas where export volumes are large and growing, such as New Orleans, tend to be less concentrated than reporting areas with smaller and declining volumes. For example, volume exported through the Atlantic Coast reporting area declined by about two-thirds over 1985 to 1998. The number of firms fell to four or less over the same period. Also, over the same period, the volume of soybeans exported through the Great Lakes reporting area increased by over 123 percent and the share of inspected exports by the four largest firms fell from 100 percent in 1990 to 71 percent in 1998.

Control of storage capacity has implications for export facilities, inland or country elevators, and overseas grain handling facilities. While storage capacity is generally not limited to only a few firms at the national or state level, local markets may be serviced by a limited number of facilities, potentially constraining farmers' storage and marketing options.

At the national level, the four largest firms account for about 27 percent of total elevator capacity. While there is much variation across states, in general, concentration tends to be lowest in those states with the largest off-farm storage capacities. Mississippi, Louisiana, and Arkansas show relatively high concentration ratios partially reflecting the exclusion of rice from the off-farm storage capacity data for these States. Federally-inspected warehouse data also do not reflect volume moving through warehouses, so concentration levels could be higher if the amount of grain handled by the larger firms is proportionately greater than their share of total elevator capacity.

Of all transportation modes, trucking is the least concentrated. While there are a couple of very large truck firms, there are no significant obstacles for entry into the trucking industry. Specialized refrigerated trucks are more problematic, but generally trucking is much less concentrated than most other industries.

There are three major barge lines covering traffic on the Mississippi River System and connecting rivers: American Commercial Barge Lines (ACBL) is the largest, followed by American River Transportation (owned by ADM) and Cargo Carriers (owned by Cargill). These three barge lines own 55 percent of the total covered barges, although there are 32 barge companies in total.

Over the period 1997–99, there have been approximately 30 mergers in the ocean freight industry. The most recent acquisition of Sealand by Maersk gives the new firm a 13 percent market share. The top ten carriers in 1990 had a market share of 33 percent, rising to nearly 50 percent today.

The top five Class I railroads accounted for 57 percent of all Class I railroad grain traffic in 1982, and by 1995, this figure had climbed to 90 percent and then to 96 percent by 1999. In addition, 95 percent of all Class I railroad revenue ton-miles in 1997 were hauled by the five largest railroads, compared to only 75 percent of Class I railroad revenue ton-miles in 1990.

Rail competition is not only a function of the number of available railroads, but also the quality and effectiveness of competitive options from the other transportation modes in particular markets. Although the number of Class I railroads has been reduced since deregulation, some have argued competition may be more intense because the remaining large railroads are stronger and their market reach is greater.

The number of route miles operated by each of the remaining Class I railroads has also increased greatly. Railroad mergers of the 1960's and 1970's combined smaller rail systems which operated in smaller geographic territories. In the 1980's, newly merged systems began to gain dominance within some geographic regions. In 1960, the average Class I railroad in the United States operated 1,956 route miles, which rose to 4,226 route miles in 1980 and to 13,313 route miles in 1998. Today, two large railroads dominate in the western United States, and two large railroads dominate in the eastern United States.

Processing.—Concentration in food processing continues to trend upward. The top four firms accounted for about 20 percent of food processing sales in 1997, compared to nearly 12 percent in 1987. The market share of the four largest firms in red meat packing rose from 47 percent in 1987 to over 60 percent in 1998. The four-firm concentration ratio for steer and heifer slaughter rose from 50 percent in 1985 to 82 percent in 2000, but has remained stable since the mid 1990s. The four largest hog slaughter firms accounted for 56 percent of total commercial hog slaughter in 2000, up from 40 percent in 1990 and 34 percent in 1980.

The number of federally inspected hog slaughter plants fell from 1,322 in 1976 to 770 in 1996. USDA's 1996 study, Concentration in the Red Meat Packing Industry, found no correlation between regional concentration and price; rather, geographic hog pricing patterns were found to be consistent with a single national market for slaughter hogs. Hogs slaughtered in large plants (those slaughtering at least 1 million head annually) and steers and heifers slaughtered in large plants (at least 500,000 head annually) continue to account for an increasing share of annual slaughter. ERS analyses found that there are economies of scale associated with these shifts in plant size, which suggests lower costs for larger plants and lower consumer prices.

Larger dairy processing firms also account for an increasing share of dairy processing. In 1998, companies with $800 million or more in sales accounted for 69 percent of U.S. dairy sales. The market share of large proprietary dairy companies increased from 39 percent in 1975 to over 42 percent in 1998, while the market share

of large U.S. dairy cooperatives increased from 17 percent to 27 percent over the same period.

Mergers and acquisitions have accounted for much of the concentration in the food processing industry. A booming economy appears to have driven the latest wave of consolidation in the food industry. Dairy processors led the number of mergers and acquisitions occurring from 1993 to the first half of 1998. Dairy processors accounted for 69 mergers and acquisitions, meat processors for 60, soft drink bottlers for 53, snack food processors for 44, and poultry processors had 32 mergers and acquisitions. Mergers and acquisitions continued into 2000. Within the 27 food or food related categories tracked by The Food Institute, merger and acquisition activity increased in 18 categories, with activity declining in 6, and remaining unchanged in 3.

Food Merchandising.—The food wholesaling sector continues to experience steady growth in sales and concentration through acquisitions. Merchant food wholesalers work with processors to distribute products to retailers and food service establishments. Mergers and acquisitions of the leading general-line grocery wholesalers have resulted in increased concentration. The top four general-line wholesalers accounted for over 40 percent of sales in 1997, up from 26 percent in 1987. Wholesalers that specialize in meat and poultry distribution have also experienced substantial increases in concentration over the past ten years, especially since 1992, while concentration in dairy product distribution has remained stable. As their customer base continues to decline due to rapid consolidation by supermarket chains, many grocery wholesalers continue to acquire retailers. In addition, concentration has also become international in scope as companies from outside the United States acquire U.S. food wholesalers. Both consolidation and international trends are expected to continue.

Mergers and acquisitions in food wholesaling can lead to efficiency gains that reduce costs and provide flexibility to offer more variety to customers within a market region. Furthermore, by growing in a familiar geographic region, a company can gain a better understanding of the consumer. By vertically expanding into retail markets, companies attempt to create synergies that reduce operating costs.

Retailing.—Widespread consolidation within food retailing has increased the share of total grocery store sales accounted for by the largest firms. Between 1990 and 1999, the market share of the largest 20 food retailers increased from 39 percent to 52 percent. Much of the increase in concentration took place between 1997 and 1999 when almost 3,500 supermarkets were purchased, representing $67 billion in sales. Analysis by ERS of the 100-largest U.S. cities found that increases in local market concentration has been moderate. In the 100 largest U.S. cities, the market share of the four largest food retailers rose from 69 percent in 1992 to 72 percent in 1998.

A number of forces have led to food retail consolidation including slow growth in annual grocery store sales, increased spending for prepared foods and meals away from home, and growth of food sales by nontraditional retailers. During the 1990's, grocery store sales, adjusted for inflation, grew about 1 percent annually.

With incomes rising, consumers increased their preference for greater convenience by purchasing more prepared foods and more meals outside the home.

These trends help to promote a competitive food retailing industry.

The expansion of retail food sales by discount mass-merchandise, warehouse club, and convenience stores has provided additional sources of competition for traditional food retailers. Mass merchandisers such as Wal-Mart, Kmart, and Target, and warehouse club store operators such as Costco, Sam's, and BJ's have increased their share of retail food sales from 5 percent in 1992 to 8 percent in 1998, while traditional food stores' share of retail food sales fell from 85 to 80 percent of sales over the same period. Further expansion of mass merchandisers in the retail food business is expected to increase their market share of retail food sales over the next several years.

Increasingly, consolidating retailers are using supply-chain management practices, which are activities coordinated with suppliers that generate operating, procurement, marketing, and distribution efficiencies, to reduce costs. Retailers claim that expected efficiency gains and lower investment requirements will allow them to maintain profitability and allow them to compete with mass-merchandiser, warehouse club stores, and other potential rivals. Retailers are likely to continue to consolidate through mergers and acquisitions in order to maintain profitability as competition heightens for the consumer food dollar.

ECONOMIC ISSUES RAISED BY CONCENTRATION

Economic growth in an industry involves business formation and expansion, mergers, acquisitions, alliances of various kinds, and exits. These dynamics of change in a market-oriented economy, such as ours, have generally resulted in consumer products more efficiently produced and of higher quality and lower price than otherwise. Nevertheless, economists cite several concerns with concentrated markets.

One issue is the extent to which increasing market concentration reduces competition and increases the ability of firms to exercise market power. Firms with market power are able to capture a larger return by offering consumers higher prices for goods of the same or even lower quality. Such behavior may persist unless other firms emerge to offer lower priced, better products. Likewise, concentrated buyers may depress prices paid to their suppliers below competitive levels and may shift costs to their suppliers by demanding that suppliers provide certain services. In addition, increasing concentration may facilitate collusion or other relationships between firms that inhibit competition, resulting in higher prices being paid by consumers.

An important limitation to market power in any industry are the possible actions of existing competitors, which could include producers of substitute products, and the potential for new competitors. Price distortions and market inefficiency, as reflected in abnormally large returns on investment, can be an incentive for entry of new competitors. Even when concentration is high, the potential threat of new entrants may prevent firms in a concentrated industry from maintaining high prices.

A second issue is the extent to which increasing concentration reduces product innovation and development. Imitation of new technologies is usually cheaper and quicker than conducting the basic research needed to develop and bring new products to market. In concentrated markets, product improvement may not be as necessary to maintain market share, so firms may not be as inclined to invest in research and product development. On the other hand, increasing concentration does not necessarily mean less investment in research and new products. Increasing concentration may enhance investment in new technologies, since larger firms may be more able to obtain the capital and human resources to fund research and market development programs.

A third issue is the extent to which increasing concentration affects the ability of sellers, such as farmers, to find markets for their products. This issue has been raised with respect to the livestock and poultry industries where some producers have concerns that their ability to independently raise animals and market them in traditional cash markets is declining.

A fourth issue is market transparency. As markets consolidate horizontally and vertically, access to market information could also decline. As information continues to increase in importance as a means to reduce costs and improve decisionmaking, lack of timely, relevant information on market conditions becomes a competitive disadvantage.

Analysis of the effect concentration has on the prices received or paid by farmers has been mixed. One broad indication of concentration often cited is the farmers' declining share of retail food expenditures. The farm-to-retail price spread—the difference between the farm value and the retail price of food—rose 5 percent in 1999, reflecting changes in the structure of the food marketing system, consumer demand for food, along with higher prices for marketing inputs, such as labor and energy. The nominal farm-to-retail price spread for all food products rose 41 percent during the last decade. In real terms, the farm-to-retail price spread for food increased 11 percent over the past 10 years. Higher costs for labor, packaging, energy, transportation, and other marketing inputs pushed the farm-to-retail spread wider, but increases in productivity can partially offset these higher costs. Changes in the cost of these marketing inputs, which are influenced by consumer demand for convenience and other preferences, generally have a greater effect on the retail price of food than do fluctuations in prices received by farmers. However, the relationship between farm and retail prices is more pronounced for food items that undergo little processing, such as fresh fruits and vegetables or fluid milk.

By reducing competition, concentration may result in higher consumer prices and a slower response by retail food prices when farm prices decline. While concentration in food retailing has accelerated since 1996, food-at-home prices, as measured by the CPI for all food-at-home, have fallen relative to the CPI for all items. An ERS study found that additional packing services and new products account for the rising wholesale-to-retail price spread for meats. The study could not attribute the rise in the wholesale-to-retail price spread for meat to increased concentration in the meat packing industry.

As food and agricultural markets have moved from local to regional to national to global, businesses in the food system has moved toward increasing their scale of production. While this evolution can improve coordination within the food chain and the response to changing consumer preferences, the potential for market power increases. This makes enforcement of antitrust laws increasingly important to farmers and consumers. The Grain Inspection, Packers and Stockyards Administration, the Department of Justice, and the Federal Trade Commission take seriously their responsibilities in merger enforcement actions, price fixing and market allocation, restraint of trade, and other anticompetitive practices.

That completes my testimony. I will be happy to respond to questions.

Senator COCHRAN. Thank you, Mr. Collins.

Ms. Waterfield, we'll hear from you now.

STATEMENT OF JOANN WATERFIELD, DEPUTY ADMINISTRATOR FOR PACKERS AND STOCKYARDS PROGRAMS, GRAIN INSPECTION, PACKERS AND STOCKYARDS ADMINISTRATION, DEPARTMENT OF AGRICULTURE

Ms. WATERFIELD. Thank you, Mr. Chairman. Mr. Chairman and members of the subcommittee, good morning and thank you for allowing me the privilege of speaking on behalf of the Grain Inspection, Packers and Stockyards Administration.

Ms. WATERFIELD. The Packers and Stockyard Programs is responsible for enforcing the Packers and Stockyards Act which prohibits, among other things, unfair, deceptive, fraudulent practices by market agencies, dealers, stockyards, packers, and live poultry dealers in the livestock, poultry, and meat packing industries.

I moved into the position of deputy administrator in September 2000 from USDA's Office of the General Counsel where I led litigation teams responsible for enforcing the Packers and Stockyards Act and also the Perishable Agricultural Commodities Act.

And let me say that I feel very privileged to represent the men and women of the Packers and Stockyards Programs, and I have long respected their professionalism, dedication, and their tenacity in pursuing and developing complex investigations and cases.

CONCENTRATION

I was asked to provide you with an overview on concentration today in these industries, but I also hope to provide you with a better understanding of the agency and our contributions to the livestock, poultry, and meat packing industries and ultimately the benefits we provide to American agriculture.

Our ability to address concentration is limited to our statutory authority. The Packers and Stockyards Act gives the Secretary of Agriculture the authority to regulate dealers, stockyards, market agencies, packers, and live poultry dealers who operate in interstate and foreign commerce.

Certain provisions of the Federal Trade Commission Act were made applicable to the Secretary's enforcement of the act and grant the Secretary investigatory powers.

To protect the livestock, poultry, and meat packing industries, the Act requires market agencies and dealers to register. Market agencies and dealers are required to be bonded, and market agencies, dealers, packers, and live poultry dealers must meet specific payment requirements.

To protect unpaid sellers of livestock, packers are subject to trust provisions that require packers to hold the proceeds from all live-

stock purchased in cash sales and all inventory of receivables of proceeds from meat, mean food products, or livestock products derived therefrom, to be held in trust for unpaid sellers until payment is made in full. There is a similar provision for live poultry dealers, but there is not a similar provision for livestock dealers.

The Packers and Stockyards Programs uses our statutory authority to investigate alleged and potential violations of the Act and regulations. And we prosecute violations that we find through our investigations, either directly through our administrative actions or through referral to the Department of Justice.

And while high levels of concentration cause a red flag and require additional oversight to ensure that there is no harm or injury that the act was intended to prohibit in the livestock, meat packing, and poultry industries, concentration in itself is not a violation of the act.

Firms are largely free to pursue their own economic interest by opening or closing plants, expanding into new geographic areas, adopting new technology and cost cutting innovations that are being integrated every day into livestock production and slaughter.

The Packers and Stockyards Programs, and the Department of Agriculture do not have pre-merger authority, and we don't have the authority to stop mergers from taking place.

The authority to investigate mergers and acquisitions resides with the Department of Justice and the Federal Trade Commission. And, when requested, we supply information and expertise to assist those agencies with their investigations of mergers or competitive issues involving the grain, livestock, meat packing, and poultry industries.

If we find and prove a violation of section 202 of the Act, we request sanctions that include orders to cease and desist from unlawful practices, and civil penalties.

We recognize that there are concerns about rising levels of concentration in the livestock and meat packing industries leading to fewer competitive marketing opportunities for producers. However, again, the Packers and Stockyards Act does not prohibit concentration.

Concentration has remained fairly constant since 1996 in the meat packing industry, but we recognize that looking further in the past, that concentration in both the cattle and hog slaughtering industries has increased greatly since 1985.

PACKERS AND STOCKYARDS PROGRAMS' INITIATIVES

In the past few years, the Packers and Stockyards Programs has been in a state of dynamic change. During fiscal year 2000, for example, the reorganization and filling of crucial positions within the Packers and Stockyards Program was completed. We utilized cross-regional expertise to address national issues, and we're looking more effectively now at emerging technology, evolving, marketing strategies and other issues affecting the industries and the constituencies we serve.

We're monitoring the livestock meat packing and poultry industries which are estimated by the Department of Commerce in fiscal year 2000 to have an annual wholesale value of $142 billion.

At the close of calendar year 2000, there were 1,318 stockyards, 6,195 marketing agencies and dealers, more than 2,000 packer buyers registered with the Packers and Stockyards Programs. There are an estimated 6,000 slaughtering and processing packers subject to the Act.

Also, in fiscal year 2000, 266 slaughtering packers, each of whom purchased more than $500,000 worth of livestock in 1999, were required to be bonded and file annual reports with us.

In addition to that, 205 poultry firms, live poultry dealers, and a significant number of meat distributors, brokers, and dealers were subject to the Act.

Last year we conducted more than 1,800 investigations of potential violations of the Act which was a 33 percent increase over the previous year.

Last year we returned more than $15 million to the industry, to our stakeholders, as a result of our custodial audits, in working with insolvent dealers, market agencies, and packers to correct their insolvencies, and in one poultry trust.

This year, halfway through the fiscal year, we've returned $14.6 million to the industry, and through a case that we initiated against a major meat packer, that meat packer reportedly returned $3 million to hog producers that it underpaid as a result of failing to disclose a change in a formula used to estimate lean percent that it purchased on a carcass basis without notifying its producers.

Last year we sent 15 rapid response teams out as a result of complaints we received in nine States, and those rapid response teams helped recover more than $3 million for growers and producers.

This year we've had 20 rapid response teams out, 2 of them are out right now. We've returned more than $2.5 million as a result of those rapid response teams.

We recognize that our regulatory responsibilities are at the heart of our mission. And to this end we closely monitor practices that may impede the trade of livestock, meat, and poultry.

We place a high priority on investigating all complaints and further developing information we receive concerning allegations of anticompetitive, unjustly discriminatory or unfair practices in the livestock, meat packing, and poultry industries.

The agency also maintains a 24-hour hotline on which constituents may anonymously voice their concerns. We respond to and investigate all issues addressed by the callers. Last year we responded to 140 calls compared to 126 in 1999, and those were in addition to the calls we receive every day in our three regional offices as well as in many headquarters.

We're also strengthening our investigations and assessments of the competitive implications of structural changes in the livestock, meat packing, and poultry industries. To further this initiative, we're currently involved in six cooperative research agreements which we anticipate will all be completed this year.

We're also involved in rule-making initiatives. We anticipate publishing our final rule on the swine contract library later this year. We're working on implementing the recommendations that were made in the GAO report that was published last year. We in-

tend to implement all of the recommendations by November of 2001.

We currently have eight cases scheduled for hearing. We have 40 cases being reviewed by the Office of the General Counsel to see if there is sufficient evidence to go forward to filing a complaint. We have 14 cases in headquarters being reviewed by our branch chiefs for referral down to the Office of the General Counsel.

We have three competitive investigation work plans being reviewed which we will work with the Office of the General Counsel if we decide to go forward with them.

And in addition to that, we are continuing to develop and retain well qualified and talented staff to enhance our ability to address complex industry issues.

PREPARED STATEMENT AND ADDITIONAL SUBMITTED QUESTIONS

Mr. Chairman and members of the subcommittee, I want to thank you again for the privilege of addressing you and representing the Packers and Stockyards Programs. If you have any further questions, I'll be happy to entertain them. If there are any questions that I cannot address at this hearing, I'll be happy to take your questions, research them further, and get back to you at a later date. Thank you.

Senator COCHRAN. Ms. Waterfield, thank you.

[The information follows:]

PREPARED STATEMENT OF JOANN WATERFIELD

Mr. Chairman and members of the Committee, good afternoon and thank you for allowing me the privilege of speaking on behalf of the Grain Inspection, Packers and Stockyards Programs (GIPSA). I am JoAnn Waterfield and I am the Deputy Administrator for GIPSA responsible for oversight of the Packers and Stockyards Programs (P&SP). The P&SP is responsible for enforcing the Packers and Stockyards Act (the Act) which prohibits unfair, deceptive, fraudulent practices by market agencies, dealers, stockyards, packers and live poultry dealers in the livestock, poultry, and meatpacking industries. I moved into this position in September 2000 from USDA's Office of the General Counsel where I led litigation teams responsible for enforcing the Packers and Stockyards Act. I feel privileged to represent the men and women of P&SP and have long respected their professionalism, dedication, and tenacity in pursuing and developing complex investigations and cases. I was asked to provide you with an overview on concentration today, but I also hope to provide you with a better understanding of the Agency and its contributions to the livestock, poultry and meatpacking industries and ultimately its benefit to American Agriculture.

Our ability to address concentration is limited to our statutory authority. P&SP has responsibility for addressing issues relating to competition and unfair trade practices in the livestock, meatpacking, and poultry industries through our authority to enforce the Packers and Stockyards Act of 1921, as amended and supplemented. The Act gives the Secretary of Agriculture the authority to regulate dealers, stockyards, market agencies, packers, and live poultry dealers who operate in interstate and foreign commerce. The Act makes it unlawful for a regulated entity to engage in unfair, unjustly discriminatory or deceptive practices. Engaging in any course of business for the purpose or effect of manipulating or controlling prices, creating a monopoly, or restraining commerce is also a violation of the Act.

Certain provisions of the Federal Trade Commission Act were made applicable to the Secretary's enforcement of the Act and grant the Secretary investigatory powers, including the power to gather and compile information, concerning the organization, business conduct, and practices of regulated entities, and to require by subpoena the attendance and testimony of witnesses in investigations.

To protect the livestock, poultry, and meatpacking industries, the Act requires market agencies and dealers to register; market agencies, packers, and dealers to be bonded; and market agencies, dealers, packers, and live poultry dealers to meet specific payment requirements. To protect the unpaid sellers of livestock, packers

are subject to trust provisions which require that all livestock purchased in cash sales, and all inventories of, or receivables of proceeds from meat, meat food products, or livestock products derived therefrom, be held in trust for the unpaid sellers until payment is made in full. There is a similar provision for live poultry dealers, but none for livestock dealers.

P&SP uses its statutory authority to investigate alleged and potential violations of the Act and regulations, and prosecute violations detected through those investigations, either directly through administrative actions or through referral to the Department of Justice.

Concentration is not prohibited by the Act, and while high concentration levels gave a "red flag' requiring additional oversight to ensure that there is no harm or injury that the Act was intended to prevent in the livestock, meatpacking and/or poultry industries. Concentration is not, in and of itself, a violation of the Act. Firms are largely free to pursue their own economic interests by opening or closing plants, expanding into new geographic areas, adopting new technology, and cost-reducing innovations that are being integrated into livestock production.

Since P&SP does not have pre-merger existing authority, PS&P does not have the ability to stop mergers from taking place. The authority to investigate mergers and acquisitions resides with the Department of Justice and Federal Trade Commission, and, as requested, GIPSA supplies information and expertise to these Agencies in any investigations of mergers or competitiveness issues involving the grain, livestock, and poultry industries.

If, however, packers engage in any of the acts prohibited by Section 202 of the Act, GIPSA investigates and initiates enforcement actions. Upon a finding of violation of Section 202, the Act provides for sanctions that include an order to "cease and desist" from the prohibited practice, and a civil penalty.

There is concern about the rising levels of concentration in the livestock and meatpacking industries leading to fewer competitive marketing opportunities for producers. Concentration has remained fairly constant since 1994. However, if you look further in the past, concentration in both cattle and hog slaughter has increased greatly since 1985. The following chart provides an historic perspective of the trends I have described.

FOUR-FIRM CONCENTRATION IN MEATPACKING, 1980–2000

[Percent of total commercial slaughter]

Year	Cattle [1]	Steers & heifers	Cows & bulls	Hogs	Sheet & lambs
1980	28	36	10	34	56
1981	31	40	10	33	53
1982	32	41	99	36	44
1983	36	47	10	29	44
1984	37	50	11	35	49
1985	39	50	17	32	51
1986	42	55	18	33	54
1987	54	67	20	37	75
1988	57	70	18	34	77
1989	57	70	18	34	74
1990	59	72	20	40	70
1991	61	75	20	44	72
1992	64	78	24	44	71
1993	67	81	25	43	73
1994	69	82	25	45	73
1995	69	81	28	46	72
1996	66	79	29	55	73
1997	68	80	31	54	70
1998	70	81	33	56	68
1999	70	81	32	56	68
2000	69	82	32	56	67

[1] Includes steers, heifers, cows, and bulls.

Note: All figures for years 1980 through 1990 are based on firms' fiscal years as reported to GIPSA. Figures for 1991 through 2000 are based on calendar year federally-inspected slaughter.

For the past few years, P&SP has been in a state of dynamic change. During fiscal year 2000, the reorganization and filling of crucial positions within the Packers

and Stockyards Programs was completed. The agency now employs a total of 180, in three species-specific regional offices (Atlanta—Poultry, Des Moines—Hogs, and Denver—Cattle and Sheep) that are directed by headquarters in Washington D.C. A full contingent of legal specialists (all of whom are attorneys), economists, and financial specialists has been established. An intensive training program and a multidisciplinary approach to developing investigation plans have also been developed. Economists now on staff provide insight and guidance in developing, analyzing and explaining complex econometric models used by the Agency in performing its regulatory responsibilities, including litigation and market oversight.

P&SP utilizes cross-regional expertise to address national issues and to look more effectively at emerging technology, evolving marketing strategies, and other issues affecting the industries and the constituencies we serve. For example, we have a cross-regional team looking at electronic transactions involving livestock. This team is comprised of representatives from each regional office with differing, but complementary areas of expertise . . . financial, legal, and economic.

P&SP monitors the livestock, meatpacking, and poultry industries, estimated by the Department of Commerce in fiscal year 2000 to have an annual wholesale value of $142 billion. At the close of 2000, there were 1,318 stockyards, 6,195 market agencies and dealers, and 2,039 packer buyers registered with P&SP. An estimated 6,000 slaughtering and processing packers are subject to the Act. In fiscal year 2000, 266 slaughtering packers, each of whom purchased over $500,000 of livestock in 1999, were required to be bonded and file reports with GIPSA. In addition, 205 poultry firms and a significant number of meat distributors, brokers, and dealers are subject to the Act.

Last year, P&SP conducted over 1,800 investigations of potential violations of the P&S Act, a 33 percent increase over the previous year. Most violations were corrected voluntarily, resulting in livestock and poultry producers receiving payment for the sale of their products. During fiscal year 2000, 17 administrative or Federal court complaints were issued (a net increase of 5 over the previous year) to bring subject firms into compliance with the Act. In addition, USDA issued 13 decisions and orders against 21 individuals or firms for violating the Act.

P&SP continues to provide payment protection to livestock and poultry producers. Financial investigations conducted last year resulted in $5.9 million being restored to custodial accounts established and maintained for the benefit of livestock sellers. This is more than double fiscal year 1999 restoration figures of $2.7 million. Since the 1976 amendments to the Act, livestock sellers have been paid $59.7 million under the Act's statutory trust provision. In 2000, one poultry trust complaint received by GIPSA resulted in payment of $250,000 to live poultry growers. By comparison, there were none in 1999. During fiscal year 2000, 192 insolvent dealers and market agencies corrected or reduced their insolvencies by $6.7 million, an increase of more than $2 million from the previous year. Insolvent packers corrected or reduced insolvencies by $2.2 million.

Our regulatory responsibilities are at the heart of our mission. To this end, P&S closely monitors practices that may impede the trade of livestock, meat, and poultry. We place a high priority on investigating all complaints and further developing information received concerning allegations of anti-competitive, unjustly discriminatory, or unfair practices in the livestock, meatpacking, and poultry industries. Appropriate corrective action is initiated when evidence of these practices is discovered.

Rapid Response teams continue to address urgent industry issues and are deployed when a situation warrants immediate attention or action. The ability of these teams to respond within 36 to 48 hours of being notified of a crisis provides the public with more immediate notification of problems with a stockyard or market agency. Last fiscal year, 15 teams were deployed to investigate cases in 9 states. Teams helped recover more than $3 million for growers and producers. The Agency also provides a hotline (1–800–998–3447) on which constituents may anonymously voice their concerns. P&SP responds to and investigates all issues addressed by the callers. Last year, the Agency responded to 140 calls, compared to 126 in 1999.

P&SP is also strengthening investigations and assessments of the competitive implications of structural changes in the livestock, meatpacking, and poultry industries. To further this initiative, P&SP entered into five cooperative research agreements in fiscal year 1999. Two examine competitive conditions in beef markets, two address competitive issues and compensation methods used in broiler production in the poultry industry, and the final project examines bidding behavior in a laboratory setting to gain insights into expected behavior in actual cattle markets. These projects will be completed in fiscal year 2001 and fiscal year 2002.

We have several hearings currently scheduled—at least two in June—and two major cases, against two of the largest packers in the Nation. The first involves a

firm alleged to have violated the Act by failing to notify sellers that it had changed its equation for estimating the lean percent of animals purchased on a carcass merit basis. We allege that as a result of this change the company underpaid more than 1,250 farmers by about $1.8 million. The second case alleges that a company retaliated against a feedlot for publishing a letter critical of the company by failing to bid or purchase from the feedlot. P&SP has incurred major litigation expenses and resources preparing for each of these cases. We have spent almost $.5 million in litigation expenses in the first case I described.

In addition to normal regulatory duties, P&SP has been tasked with four Congressional Mandates, which will impact the Agency next year, and in subsequent years. They are the Swine Contract Library, Captive Supply Study, an Annual Assessment of the Cattle and Hog Industries, and the Agency's implementation of the General Accounting Office's recommendations in last year's report.

1. The first mandate, the Swine Contract Library, set out in the Agricultural Rural Development, Food and Drug Administration, and Related Agencies Appropriations Act of 2000 (Public Law 106–78) was signed into law on October 22, 1999. It amended the P&S Act to require P&SP to establish and maintain a library of contract provisions offered by packers to swine producers for the purchase of swine and to make that information available to the public. The swine contract library must include contracts from swine packing plants with a slaughter capacity of 100,000 swine or more per year; this includes approximately 50 plants owned by 29 packers which account for over 95 percent of the market. In addition to providing all hog purchase contracts to P&SP, these 29 packers are required to provide monthly reports to P&SP specifying the number of swine committed and the maximum number of swine to be delivered over the next six to twelve months by contract type.

GIPSA published a Notice of Proposed Rulemaking on September 5, 2000 to implement the Swine Contract Library and is drafting the final rule. In addition to the rulemaking process, P&SP has devoted resources to implement the actual contract library, involving computer hardware and software development, and data collection forms. The library will use a Web-based system to facilitate real-time data input from swine packers and data access by the public.

2. The second mandate arising out of last year's appropriations bill, is in a Conference Report (House Report No. 106–948) that directs GIPSA to complete a comprehensive study on Captive Supplies by September 30, 2001. The report will examine and report on whether or not cattle that are procured pursuant to a captive supply arrangement by a packer's non-reporting subsidiary, affiliate and owners, officers and employees are being included in the cattle reported as captive supply. Additionally, the report will explain differences in the volume of captive supplies reported in the P&SP Annual Statistical Report and those reported by other entities. Because of the scope of the report and the requirements of the Paperwork Reduction Act, we will not be able to complete this report by September 30th of this year, however, we will provide Congress with an interim report consisting of qualitative analyses that are descriptive of the issues.

3. The third mandate requires the Agency to submit an annual report to Congress that assesses the cattle and hog industries. The Packers and Stockyards Act was amended in the Grain Standards and Warehouse Improvement Act of 2000 (Public Law 106–472) to require the Agency to submit an Annual Report Assessing the Cattle and Hog Industries. The report will include an assessment of the general economic state of the cattle and hog industries, changing business practices in these industries and practices that appear to raise concerns under the P&S Act. We estimate that 2,000 staff hours and $72,000 were spent in compiling this report for 2000.

4. The final mandate began with the General Accounting Office's (GAO) Report to Congress, issued in September 2000, "Actions Needed to Improve Investigations of Competitive Practices." The Grain Standards and Warehouse Improvement Act of 2000 (Public Law 106–472) required implementation of the recommendations in the GAO Report as well as a report describing the actions taken to improve investigations of competitive practices by November 9, 2001.

The GAO report addresses actions to improve P&SP's ability to investigate complex issues. The report recommends that the Secretary of Agriculture develop a teamwork approach with P&SP economists and the Office of General Counsel (OGC) attorneys for complex investigations. We began implementing this recommendation a month after the September report with combined competition training for legal specialists, economists, and OGC attorneys. P&SP now has two legal specialists in each regional office, who have recently completed training provided by OGC. We have formalized procedures within P&SP by instituting investigation reviews by senior management when cases involve competition issues, are complex, are large, involve more than one unit (financial, competition, trade practices), involve more

than one region, or require unusual resources. A regional legal specialist reviews each investigation plan before it is submitted for consideration to senior P&SP management. Once senior management has reviewed and approved each investigative plan, the investigation proceeds. Each case is monitored throughout the investigation. OGC reviews complex investigation plans prior to commencement of the investigation and thus has been integrated into the investigative process of complex cases.

The GAO report recommended that GIPSA improve its competitive investigations by adopting methods and guidance similar to those used by the Department of Justice (DOJ) and the Federal Trade Commission (FTC). GIPSA, working through the Department's Office of the General Counsel, is reviewing DOJ and FTC investigative procedures.

The GAO report recommended that the Secretary modify the grade structure for economists. The process of upgrading economists' and legal specialists' positions is underway and should be completed shortly.

The GAO report also recommends that GIPSA provide industry participants and Congress with clarifications of the Agency's views on competitive activities by reporting changing business practices in the cattle and hog industries and by identifying market operations or activities that raise concerns. We have strengthened our commitment to communicate our policies more clearly and effectively to our stakeholders. We will publish an annual report assessing the cattle and hog industries. We are in the process of hiring an outreach coordinator to improve our communication with Congress and the public we serve.

In addition to the Congressional mandates, P&SP will be participating in a GAO investigation initiated by Senator Daschle to examine USDA's econometric models. He has asked the GAO to "assess the extent to which these models may be understating the effects of imports, market concentration, and the use of marketing agreements and forward contracts on domestic cattle prices." Senator Daschle has also requested that GAO provide recommendations on how USDA models could be "improved or revised, to provide the most comprehensive analysis possible of the impact of certain factors on prices at the producer level, including: import volumes and competition; increasing use of marketing agreements and forward contracts; and increasing consolidation in the processing, wholesaling and retail distribution sectors." We fully expect GAO to review the 1996 packer concentration study, the follow-up cooperative agreements with universities that examined concentration and captive supplies, and other activities relating to concentration and captive supplies. GAO expects to complete its investigation within one year.

While working to be wholly responsive to Congressional mandates and to provide timely information to GAO, P&SP has initiated the development of regulations to help us better serve our various constituencies. The regulations will support our enforcement of the Act. We are currently working on several rulemaking initiatives.

P&SP will actively seek to serve the industry by: providing payment protection to livestock and poultry producers; increasing the number of investigations of potential competitive violations of the Act; pursuing voluntary corrections of violations of the Act that will result in livestock and poultry producers receiving additional funds; continuing to reach out to both educate and inform constituencies served by the Agency of the benefits and protections offered to livestock and poultry producers; monitoring and responding rapidly to complaints of anticompetitive, unjustly discriminatory or unfair practices in the livestock, meat and poultry industries; pursuing cooperative agreements that contribute valuable information to P&SP's understanding of the industries; facing-off with industry giants and expending resources to correct violations of the Act; responding thoroughly and responsibly to all governmental and Congressional mandates; and pursuing rulemaking that enhances P&SP's ability to investigate and litigate violations of the Act. However, our ability to control or limit concentration lies solely within parameters defined by the Act and limits set therein.

P&SP teams of legal, financial, and economic specialists are currently addressing 14 cases, are working with OGC on 8 cases scheduled for hearing, and are assisting in over 40 cases which are being developed for enforcement by the OGC. In addition to managing complex cases, we will be continuing to develop and retain well-qualified and talented staff to enhance our ability to address industry issues.

Mr. Chairmen and members of the subcommittee, thank you for the privilege of addressing you and representing the P&SP. If you have further questions, I would be happy to entertain them. If I cannot address them at this hearing, I will have your questions researched further and respond directly to you at a later date.

QUESTIONS SUBMITTED BY SENATOR BYRON L. DORGAN

Question. In recent years there has been an assumption that efficiency should be the primary goal in our agribusiness production chain, but many so-called efficiencies gained by concentrated entities are actually externalized costs shifted from the company to the communities that must supply medical care for uninsured labor, increased education costs for immigrant families, and environmental problems resulting from concentrated production systems. Why haven't you measured the full cost of production in these efficiency gains of these concentrated companies?

Answer. In a market-based economy, business structures undergo constant evolution, reflecting the emergence of new technology and new profit-making opportunities. Over the past several years, markets have generally become more concentrated and this trend is not unique to agricultural markets. Despite increasing levels of concentration across many markets, environmental problems and other market externalities, for the most part, do not appear to have escalated appreciably. This observation is not based on an exhaustive industry-by-industry study of agribusiness firms but a reflection of the lack of pressure on policymakers for new environmental laws and regulations. While it may be useful to conduct in-depth industrial studies of the evolution and transformation of companies and industries and of the indirect effects that occur over time, including estimates of external costs, such as medical, education, and environmental costs, these effects are difficult to measure and may have limited application. Therefore, we are focusing our research resources on areas where we believe results can be obtained most cost effectively.

Question. Why aren't externalized costs part of how USDA measures gains and losses particularly in the processing sector?

Answer. As indicated above, there is merit in conducting in-depth industrial studies of the evolution and transformation of companies and industries and of the direct and indirect efficiency gains or losses that occur over time, including estimates of external costs. Estimates of externalized costs would necessitate site-specific information on production and hiring practices, air and water quality, and possibly other environmental indicators. Using these environmental and other indicators, methods would have to be developed to estimate the direct and indirect costs imposed on society by an agribusiness processing firm. At the present time, there are no widely accepted methods for estimating the cumulative sum of these costs. Such activities would be costly and compete for limited research resources. Thus, our research priorities are focused on areas where we believe we can have the greatest impact for our research dollar.

Question. For some time we have had an increase between what the producer receives and what the consumer pays at the counter for food. Why does USDA continually ignore the increasing pressure from both the processing and retail sectors on both the commodity price and the price the consumer pays?

Answer. USDA data indicates that farmers' share of the retail food dollar has declined by over 50 percent since the early 1970's. Over the same period, concentration levels have increased in food processing and retailing. While some may conclude from the two trends that increasing concentration is at least partially responsible for the drop in the share of the retail food dollar going to farmers, correlation does not necessarily imply causation. In fact, many economists argue that the decline in the farmers' share of the retail food dollar reflects consumers steadily increasing preference for convenience foods that require special processing and packaging. The rising preference for convenience foods is an outgrowth of higher income levels and rising employment of both spouses outside the home. Another factor behind the declining farm share of the retail dollar is the rapid productivity growth in production agriculture compared with productivity growth in food processing and transportation.

Question. To just simply say we pay such a low percentage for food on a global comparison, when we have the largest disposable income in the world, doesn't mean that consumers aren't being unfairly charged for their purchases, does it?

Answer. You are correct. Comparing the percentage of income spent on food by U.S. consumers relative to consumers in other countries does not indicate whether consumers in this country are being overcharged.

Question. Why does USDA consistently return to the same economists for so-called independent research on captive supply and market concentration?

Answer. We've made every effort at USDA to elicit comments and research on captive supplies and market concentration from all interested parties. USDA has held two forums on captive supplies and market concentration over the past couple of years. At each of those forums, all interested parties were invited to participate. If you know of any individuals that have conducted recent research on captive sup-

plies and market concentration that we may not be aware of, we would appreciate receiving those reports and meeting with those individuals.

Question. Why aren't you using economists from universities outside of the traditional land grants?

Answer. This question appears to relate to economic research related to captive supplies and market concentration. As indicated in the response to the previous question, we've made every effort at USDA to elicit comments and research from all interested parties and from economists both inside and outside of the traditional land grants. An example would be the diverse peer reviewers we used for the Texas fed cattle procurement studies.

Question. Do you check the background of the economists you award grants to, to make sure they are independent of the entities they are researching? Answer. USDA awards research grants to economists who are recognized in their field of study and have a history of publishing peer-reviewed research. Individuals receiving grants are noted by their peers as conducting leading-edge, independent research in their field of expertise. The Department does not conduct background checks, but checks are made to see whether an individual received funding in the past from an entity that they are researching. Each potential applicant for an award is requested to disclose their funding sources.

Question. Given that a truly competitive market requires meaningful choice by producers for marketing outlets, would you agree that the market at the farm gate is almost non-existent in many parts of the country?

Answer. In some parts of the country the number of buyers of farm products and sellers of farm inputs may be limited. However, new and emerging marketing outlets are creating new marketing opportunities for farmers and ranchers. For example, we are seeing the re-emergence of farmers' markets as a viable market for some producers. And, the internet is greatly expanding the availability of market information and the potential market for some products. Through the internet, farmers and ranchers do not have to be restricted to buying from their local farm input supplier or selling to the local cattle or grain buyer. In addition, increasing availability of market information through the internet and other sources, provides farmers and ranchers with information on which to judge whether local prices offered by farm input sellers and buyers of grain and cattle are fair. Increasing market information may also motivate local buyers and sellers to offer fair prices to farmers and ranchers.

Question. Most every Federal agency that does investigations utilizes investigators that have legal training so they can analyze facts in light of whether the law has been violated. However, USDA–GIPSA uses economists with little or no legal training to perform investigations. Would you agree that one reason that GIPSA has been hampered in its enforcement duties is that it has not utilized investigators which are trained in the law, especially the Packers and Stockyards Act?

Answer. I do not agree that GIPSA's enforcement duties have been hampered because investigators are not trained in the law, especially the Packers and Stockyards Act. While an economist's academic training alone does not prepare them to perform investigations, GIPSA's economists undergo rigorous training programs once they come on board. The objectives of these training programs are to help investigators identify violations of the Packers and Stockyards Act and perform investigations working in conjunction with other agencies, such as USDA's Office of General Counsel and the Department of Justice.

ATTORNEYS EMPLOY BY PACKERS AND STOCKYARDS PROGRAMS

Question. How many attorneys will be directly employed by Packers and Stockyards Programs—not general to USDA but specifically assigned to P&S?

Answer. The Packers and Stockyards Programs (P&SP), Grain Inspection, Packers and Stockyards Administration, has seven legal specialist positions (one position is temporarily vacant at the present time). All legal specialists employed by P&SP are licensed attorneys. There are two legal specialists in each of the three regional offices, and a supervisory legal specialist in the P&SP Washington headquarters office. The supervisory legal specialist reports directly to the P&SP Deputy Administrator, who is also a licensed attorney. The duties of the legal specialists include: (1) participating in investigation planning and execution; (2) consulting with the Office of the General Counsel (OGC) attorneys; (3) conducting research; and (4) reviewing P&SP correspondence. Additionally, the OGC Trade Practices Division provides all legal services to P&SP. Trade Practices currently has twelve attorneys who provide legal services to two programs, P&SP and the Perishable Agricultural Commodities Branch of the Agricultural Marketing Service.

Question. That compares to how many attorneys from IBP or Cargill for example?

Answer. P&SP does not have access to information about how many attorneys are employed by either IBP or Cargill. During the litigation of the IBP case in 1997, IBP had six attorneys present at the administrative hearing.

ACCOUNTANTS VERSUS ECONOMISTS

Question. In the past we've relied heavily on economists for analysis on potential price fixing in the packing sector. Economists, however, tend to use complicated formulas unreadable by the lay public to "study" the possibility there may be price fixing. Isn't it more logical to use accountants who can provide a more direct, substantive analysis of figures that can be made understandable to the public and therefore more intelligible to a jury, instead of just general, industry-wide assumptions as we often see in the econometric formulas USDA puts out?

Answer. Cases in which P&SP has alleged violations by packers of section 202 of the Packers and Stockyards Act are tried before an Administrative Law Judge in an administrative hearing. There is no jury in those proceedings. Enforcement of section 202 alleging violation by a live poultry dealer (processor) is through referral to the Department of Justice and trial in Federal court where there may be a jury trial. In preparation for litigation, P&SP economists work closely with OGC attorneys to ensure evidence is presented in a clear, logical fashion that is understandable. Economic formulas are sometimes necessary to demonstrate causal relationships and/or harm to producers. During the investigation of a case, P&SP legal specialists and OGC attorneys work with the economists to ensure the data and evidence that are necessary for the analysis is collected and after referral of the case to OGC, the economists work with OGC to ensure that the analysis is presented in clear and concise exhibits introduced by appropriate witness explanation and clarification. Auditors and accountants, including certified public accountants, are used in investigative teams, as are marketing specialists, but auditing and accounting theory and practice are not always adequate to prove causality and/or effects of economic behavior such as price fixing, with the attendant economic and competitive harm. One of the principal findings of the 1997 USDA Office of the Inspector General investigation was that P&SP needed economists to prepare economic models to demonstrate the adverse effects of anticompetitive behavior in the marketplace. P&SP has formalized a teamwork approach to ensure that GIPSA's economists, legal specialists, auditors and marketing specialists work with OGC to identify and prove violations of the Packers and Stockyards Act.

TRANSFER TO THE DEPARTMENT OF JUSTICE

Question. From your experience and knowledge of P&S and its internal and external problems, should it be moved from USDA?

Answer. We believe P&SP can best address livestock and poultry industry problems and regulate individuals and businesses subject to the P&S Act as part of USDA. P&SP's collective expertise and experience within USDA is essential to its continued effectiveness in the regulation of the livestock, meatpacking, and poultry industries. We do agree that P&SP can improve its effectiveness by studying other agencies' investigative procedures, such as the procedures used by the Department of Justice and the Federal Trade Commission. P&SP is reviewing investigative procedures used by these agencies to improve its investigations of anticompetitive practices. As part of OGC's training of legal specialists in March, 2001, attorneys from the Federal Trade Commission conducted a training session for P&SP legal specialists, computer specialists, economists and recently hired OGC attorneys on procedures for requesting and obtaining electronic records for investigations.

Question. (1) How many major cases can you handle at once? (2) How many attorneys are working on competition issues under the P&S Act? (3) Would you object to the creation of an Office of Agriculture in DOJ to address not only antitrust issues in agriculture generally, but to have dual jurisdiction over the trade practices portion of your jurisdiction under the Packers & Stockyards Act?

Answer. (1) We have the capability of handling multiple cases of varying degrees of complexity at one time. Since each case differs with regard to its level of complexity and its requirement of human and fiscal resources, it is not possible to answer the question of how many competition cases we could handle with exactness. For example, we could handle two cases in the investigation state and two in the briefing stage while there were two in litigation. We estimate that only two complex cases could be handled simultaneously in active litigation, which presumes administrative hearings held concurrently. (2) All P&SP legal specialists (seven positions) and OGC Trade Practices Division attorneys (12 attorneys) spend a significant amount of time working on competition issues under the P&S Act. (3) P&SP takes no position regarding the creation of an Office of Agriculture in the Department of

Justice (DOJ) to handle antitrust or trade practices. P&SP works closely with the DOJ and the Federal Trade Commission (FTC) to monitor the regulated industry regarding antitrust issues. We believe P&SP currently has the experience, training, and expertise to properly enforce the trade practices portion of our jurisdiction, as well as the competition and financial portions. We further believe that together the existing entities of P&SP, DOJ, and the FTC do an effective job monitoring industry antitrust issues.

QUESTIONS SUBMITTED BY SENATOR TIM JOHNSON

CAPTIVE SUPPLY PROBLEM

Question. In September of 2000, USDA held a public forum on the problem of captive supply in Denver. Captive supply can include arrangements that meat packers utilize to lock-up or secure a given amount of kill needs, such as packer-owned livestock, formula or negotiated sales, or contracted production. Producers are concerned that growing captive supply results in an inactive and anti-competitive cash marketplace. What was the outcome of the forum and what does USDA plan to do to address the growing issue of captive supply in livestock markets?

Answer. At the September 2000 USDA public forum, a broad spectrum of views were presented on whether captive supplies artificially depress prices to cattle producers. Some presenters argued that captive supplies were depressing cattle prices, while the majority of economists held the viewpoint that captive supplies were not adversely affecting prices offered to cattle producers. Thus, the current available evidence, on balance, suggests captive supplies are not contributing to an inactive and anti-competitive marketplace for cattle. USDA continues to monitor captive supplies and to review analytical studies as they become available. No other action regarding captive supplies are being contemplated at this time.

BARGAINING POWER FOR PRODUCERS

Question. Given that a truly competitive market requires meaningful choices for farmers and ranchers in terms of marketing outlets, would you agree that the market at the farm-gate level is almost non-existent in many parts of the country?

Answer. In some parts of the country the number of buyers of farm products and sellers of farm inputs may be limited. However, new and emerging marketing outlets are creating new marketing opportunities for farmers and ranchers. For example, we are seeing the re-emergence of farmers' markets as a viable market for some producers. And, the internet is greatly expanding the availability of market information and the potential marketplace for farm products. Through the internet, farmers and ranchers do not have to be restricted to buying from their local farm input supplier or selling to the local cattle or grain buyer. In addition, increasing availability of market information through the internet and other sources, provides farmers and ranchers with information on which to judge whether local prices offered by farm input sellers and buyers of grain and cattle are fair. Increasing market information may also motivate local buyers and sellers to offer fair prices to farmers and ranchers.

USE OF ECONOMISTS INSTEAD OF ATTORNEYS IN INVESTIGATIONS

Question. Most Federal agencies that conduct investigations primarily utilize investigators that have legal training so they can analyze facts in light of whether the law has been violated. However, USDA–GIPSA uses economists with little or no legal training to perform investigations. Would you agree that one reason that GIPSA has been hampered in its enforcement duties is that it has not utilized investigators which are trained in the law for trade practices and competition cases, especially the Packers and Stockyards Act?

Answer. USDA's Office of the Inspector General issued a report in 1998 and the Government Accounting Office issued a report in 2000 that found that a lack of legal expertise has hampered GIPSA's investigations, particularly in complex cases such as restriction of competition investigations. GAO recommended that GIPSA work more closely with USDA's Office of the General Counsel (OGC) early in investigations. GIPSA is working to increase the role of OGC attorneys in competition investigations and include the Assistant General Counsel of OGC's Trade Practice Division in the decisions of which investigations to pursue and what evidence is necessary to pursue them. GIPSA created seven legal specialist positions within P&SP, all are licensed attorneys. The duties of the legal specialists include: (1) participating in investigation planning and execution; (2) consulting with OGC attorneys; (3) conducting research; and (4) reviewing P&SP correspondence.

Question. How many attorneys are working on competition issues under the P&S Act? Is this number adequate?

Answer. As noted above, P&SP has seven legal specialist positions; two in each of the three regional offices, and a supervisory legal specialist in the P&SP Washington headquarters office. These attorneys provide assistance to our investigators in consultation with the attorneys in OGC, and conduct research. The twelve attorneys in the Trade Practices Division of OGC provide legal services to P&S, including litigation services. All of these attorneys spend a substantial amount of time on competition issues. At this point in time, this number of attorneys is adequate to handle the cases that are being developed.

Question. How many major cases can GIPSA handle at once?

Answer. We have the capability of handling multiple cases of varying degrees of complexity at one time. Since each case differs with regard to its level of complexity and its requirement of human and fiscal resources, it is not possible to answer the question of how many competition cases we could handle with exactness. For example, we could handle two cases in the investigation state and two in the briefing stage while there were two in litigation. We estimate that only two complex cases could be handled simultaneously in active litigation, which presumes administrative hearings held concurrently.

GENERAL ACCOUNTING OFFICE REPORT ON GIPSA

Question. A September 2000 General Accounting Office Report asserted that the Grain Inspection, Packers and Stockyards Administration lacks the staff, budget, and expertise to investigate anticompetitive behavior in livestock markets, and GAO recommended (Report# RCED–00–242) that GIPSA require an earlier integration of attorneys in the planning and review of investigations and closer consultation take place between GIPSA, the Department of Justice, and the Federal Trade Commission during investigations. This will enable GIPSA to implement GAO's recommended improvements as required by the November 9, 2000 passage of the Grain Standard and Warehouse Improvement Act of 2000 (Public Law 106–472). What is the status of GIPSA efforts to comply with our Congressional mandate and GAO's recommendations to secure more attorneys and integrate those attorneys into investigations?

Answer. The General Accounting Office (GAO) issued the "Actions Needed to Improve Investigations of Competitive Practices" report to Congress in September 2000. The Grain Standards and Warehouse Improvement Act of 2000 (Public Law 106–472) requires implementation of the recommendations identified in the GAO report as well as a report describing the actions taken to improve investigations of competitive practices by November 9, 2001.

The GAO report addressed actions that will improve the ability of Packers and Stockyards Programs (P&SP) to investigate complex issues. The report recommends that the Secretary of Agriculture:

—develop a teamwork approach for complex investigations with P&SP economists and Office of the General Counsel (OGC) attorneys,
—improve competition investigations by adopting methods and guidance similar to the Department of Justice (DOJ) and the Federal Trade Commission (FTC),
—modify the grade structure for economists, and
—provide industry participants and Congress with clarifications of P&SP's views on competitive activities by reporting changing business practices in the cattle and hog industries and identifying market operations or activities which raise concerns.

Developing a teamwork approach for complex investigations with P&SP economists and OGC attorneys began one month after the September report with training in the development and use of econometric evidence for legal specialists, economists and OGC attorneys. In addition, OGC conducted a one-week training program for P&SP legal specialists in March 2001. P&SP is currently developing and implementing an investigation review plan that will include OGC in the early stages of a competition case's development and investigation. In response to additional appropriations provided by Congress for the purpose, OGC added two additional attorneys to the Trade Practices Division staff with the possibility of adding an additional two attorneys as the caseload requires. In addition, P&SP created a supervisory legal specialist position to provide for central supervision of its legal specialists. As part of the "early and often" consultation with OGC, recommended by the GAO report, OGC conducted a week long training program for P&SP legal specialists in March 2001.

We have formalized procedures within P&SP by instituting investigation reviews by senior management. This review occurs when several of the following criteria are present:

—the case involves issues of competition
—the case is complex
—the investigation is extensive
—the investigation involves more than one unit of P&SP (financial, competition, trade practices) in the investigation,
—the case involves more than one regional office
—the case would require the commitment of large human or fiscal resources

Once senior management has reviewed and approved each investigation plan, the investigation proceeds, and each investigation is monitored throughout the investigation. We ask OGC to review competition and complex investigation plans prior to commencement of the investigation.

We continue to review DOJ and FTC investigative procedures to improve our investigative procedures of alleged anticompetitive practices. P&SP has contacted DOJ and FTC staff to set the stage for further discussions. As part the OGC training for legal specialists held in March of this year, attorneys from the FTC conducted a training session for P&SP legal specialists, computer specialists, and economists and recently hired OGC attorneys on procedures for requesting and obtaining electronic records for investigations.

The process of upgrading economist positions is underway to allow P&SP to hire and retain well-qualified individuals.

We have strengthened our commitment to communicate our policies more clearly and effectively to our stakeholders. We have published an annual report assessing the cattle and hog industries. We are in the process of hiring additional staff to improve our communication with Congress and the public we serve.

We are continuing to reach out to both educate and inform constituencies served by the Agency of the benefits and protections offered to livestock and poultry producers.

PACKERS AND STOCKYARDS PROGRAMS REGULATORY PERSONNEL NEEDS

Question. Does P&S have adequate personnel on board to promulgate regulations in a timely fashion? How many reg writers does P&S currently employ?

Answer. At the present time, P&SO has one regulatory analyst. We plan to hire another program analyst with regulatory writing experience to assist with promulgating regulations and other related P&SP program activities. Due to the relatively small size and the nature of the work, few regulations are issued during the course of the year so that personnel working on regulations and rulemaking initiatives also work on congressional mandates, proposed legislation, paperwork reduction act requirements, and other program activities as needed.

CREATION OF AN OFFICE OF AGRICULTURE IN THE DEPARTMENT OF JUSTICE

Question. Would you object to the creation of an Office of Agricultural Competition in DOJ to address not only antitrust issues in agriculture generally, but to have dual jurisdiction over the trade practices and competition portion of your jurisdiction under the Packers and Stockyards Act?

Answer: P&SP takes no position regarding the creation of an Office of Agriculture in the Department of Justice (DOJ) to handle antitrust or trade practices. P&SP works closely with the DOJ and the Federal Trade Commission (FTC) to monitor the livestock, meatpacking, and poultry industries regarding antitrust issues. We believe P&SP currently has the experience, training, and expertise to properly enforce the trade practices portion of our jurisdiction over these industries, as well as the competition and financial portions. We further believe that together the existing entities of P&SP, DOJ, and the FTC do an effective job monitoring industry antitrust issues.

Senator COCHRAN. Mr. Nannes.

Mr. Nannes.

STATEMENT OF JOHN M. NANNES, ACTING ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION, DEPARTMENT OF JUSTICE

Mr. NANNES. Thank you, Mr. Chairman. I'm pleased to have the opportunity this morning to discuss antitrust enforcement in the agricultural marketplace.

As I believe you know, we are awaiting a Senate vote on the nomination of Charles James to be the Assistant Attorney General for the Antitrust Division. Until that time, the Division is deferring policy statements.

However, the Antitrust Division is first and foremost a law enforcement agency, and our enforcement work continues even during times of transition. For that reason, I thought it would be helpful to the subcommittee if I were to describe how the Division applies the antitrust laws to agricultural industries.

We know that the agricultural marketplace is undergoing significant changes. In the midst of these changes, farmers and especially family farmers have expressed concern about concentration in agricultural markets. Farmers know that antitrust enforcement is essential to assuring competitive markets.

ENFORCEMENT OF ANTITRUST LAWS

The Antitrust Division has been very active in enforcing the antitrust laws in the agricultural sector. Let me briefly describe for you some of our recent enforcement actions.

In our conversations with farm groups, we have found that farmers are especially concerned about the potential impact of mergers, so let me start there. Section 7 of the Clayton Act prohibits mergers or acquisitions that may tend to lessen competition. In the past 3 years, the Antitrust Division has challenged four significant mergers that we concluded could have harmed competition in agricultural markets.

First, we challenged Monsanto's proposed acquisition of DeKalb Genetics Corporation, which would have significantly reduced competition in corn seed, biotechnology innovation to the detriment of farmers.

Second, we challenged Cargill's proposed acquisition of Continental's grain business, which would have significantly reduced competition in the purchase of grain and soybeans from farmers in various local and regional markets.

Third, we challenged New Holland's proposed acquisition of Case, which would have significantly reduced competition in the sale of tractors and hay tools to farmers.

Fourth, we challenged Monsanto's proposed acquisition of Delta and Pine Land, which would have significantly reduced competition in cotton seed, biotechnology, once again to the detriment of farmers.

AGRICULTURAL MERGERS

Taken as a whole, I'd suggest that these enforcement actions demonstrate the following points. First, we carefully review agricultural mergers for their competitive implications.

Second, our focus is not limited to traditional agricultural products, but extends also to technology innovation.

Third, while we consider proposed divestitures to address the competitive problems that we find with a merger, we won't hesitate in challenging the entire merger if we conclude that lesser forms of relief are not sufficient to address fully the competitive problem presented by the merger.

Fourth, we'll challenge a merger, whether the likely harm is that farmers will have to pay anticompetitively high prices for the products they purchase, or that farmers will have to accept anticompetitively low prices for products they sell, as demonstrated by Cargill/Continental.

I want to emphasize this last point because I know it is a matter of particular concern to the subcommittee and to farmers who often have to sell their products to large agribusinesses.

For a while there seems to have been some uncertainty about whether we can consider a merger's possible anticompetitive harm to producers. The answer is: Cargill/Continental demonstrates is that we can and we do.

We conducted a very substantial investigation of the Cargill Continental merger. The merging parties were sellers of grain and soybeans in the United States and in international markets, and also were buyers of grains and soybeans in various local and regional domestic markets. We looked at all of the potentially affected markets.

We concluded the merger would not harm competition in the markets in which the parties were sellers. However, we did find that the merger would likely have had an anticompetitive effect in some markets in which Cargill and Continental were buyers, and could have depressed the prices received by farmers for grain and soybeans in those regions.

We challenged the merger on that basis and on that theory, and the parties resolved our concerns by restructuring the merger and agreeing to significant divestitures of port, rail, and river terminals. The district court judge to whom that decree was submitted concluded that that decree was very much in the public interest.

AGRICULTURAL CRIMINAL ENFORCEMENT ACTIONS

The Division has also brought a number of significant criminal enforcement actions related to agriculture in the last few years under section one of the Sherman Act, which makes unlawful contracts, combinations, and conspiracies in restraint of trade. Our criminal enforcement focuses on the types of agreements that are blatantly anticompetitive, such as price fixing and allocations of customers and markets.

In the agricultural sector, we have prosecuted companies that fix prices for products purchased by farmers, such as lysine and vitamins used as animal feed additives, securing numerous convictions of companies and individuals and some of the highest fines in antitrust enforcement history.

The Division also investigates other kinds of business behavior that may have anticompetitive effects. Such conduct may constitute an illegal restraint of trade or an unlawful monopolization or attempted monopolization in violation of the Sherman Act.

CIVIL INVESTIGATIONS

We have conducted a number of civil investigations in which we have considered whether conduct is having an anticompetitive impact on farmers, and if we determine that such is the case, we will take appropriate enforcement action.

The Division works hard to ensure that it is receiving the information necessary to make the best informed judgments with respect to agricultural antitrust issues.

We often obtain valuable information for our merger investigations from the USDA, and from time to time USDA has referred to us other matters that have led to criminal prosecution.

In turn, we have provided assistance to the USDA—mostly as consultants on competition-related studies, and more recently by sharing information regarding our investigative techniques to follow up on the recommendations made in the recent GAO report and subsequent legislation.

Our working relationship is reflected in a written memorandum of understanding with the USDA, and we have a very constructive working relationship with that agency as well as with other Federal agencies that have responsibilities in these areas, and the various state attorneys general.

PREPARED STATEMENT

In conclusion, the Antitrust Division understands the concerns that have been expressed about competition in agricultural markets. We take seriously our responsibility to assure that the antitrust laws are enforced no less vigorously in the agricultural markets than in the rest of our economy.

We believe our enforcement efforts demonstrate that commitment, Mr. Chairman. I would be happy to respond to any questions that you or your colleagues may have.

[The statement follows:]

PREPARED STATEMENT OF JOHN M. NANNES

Good morning, Mr. Chairman and members of the Subcommittee. I am pleased to have the opportunity to discuss issues relating to antitrust enforcement in the agricultural marketplace.

As I believe most of you know, we are awaiting a Senate vote on the nomination of Charles James to be Assistant Attorney General for the Antitrust Division. Until that time, the Division is deferring official policy statements. However, the Antitrust Division is first and foremost a law enforcement agency, and our enforcement work continues even during times of transition. For that reason, I thought it would be helpful to the Subcommittee if I were to describe how the Division enforces the antitrust laws and review how those laws have been applied in agricultural industries.

We know that the agricultural marketplace is undergoing significant change. Farmers are adjusting to challenges in international markets, to major technological and biological changes in the products they buy and sell, and to new forms of business relationships between producers and processors.

In the midst of these changes, farmers have expressed concern about the level of competitiveness in agricultural markets. Farmers know that competition at all levels in the production process leads to better quality, more innovation, and competitive prices. They know, too, how important antitrust enforcement is to ensuring competitive markets. Enforcement of the antitrust laws can benefit farmers in their capacity as purchasers of goods and services that allow them to grow crops and raise livestock, and also in their capacity as sellers of crops and livestock to feed people, not only in our country but also throughout the world.

The Antitrust Division takes these concerns seriously and has been very active in enforcing the antitrust laws in the agricultural sector.

Under Section 7 of the Clayton Act, the Division can challenge a merger or acquisition that it concludes may tend substantially to lessen competition. During the past few years, the Division has challenged a number of significant mergers that would have harmed agricultural markets, such as:

—the proposed acquisition by Monsanto of DeKalb Genetics Corporation, which would have significantly reduced competition in corn seed biotechnology innovation to the detriment of farmers;

—the proposed acquisition by Cargill of Continental's grain business, which would have significantly reduced competition in the purchase of grain and soybeans from farmers in various local and regional markets;
—the proposed acquisition by New Holland of Case, which would have significantly reduced competition in the sale of tractors and hay tools to farmers; and
—the proposed acquisition by Monsanto of Delta & Pine Land, which would have significantly reduced competition in cotton seed biotechnology to the detriment of farmers.

Under section 1 of the Sherman Act, the Antitrust Division can challenge agreements between competitors that restrain trade. With respect to the types of agreements that are obviously anticompetitive—such as price fixing and allocations of markets and/or customers—the Division often proceeds by criminally prosecuting the companies and individuals involved. In recent years, the Division has criminally prosecuted various companies for fixing prices for products purchased by farmers—lysine and vitamins—and has secured numerous criminal convictions and some of the highest fines in antitrust history. Under the Sherman Act, the Division can also proceed civilly to challenge other types of agreements or unlawful monopolies that it concludes are injuring suppliers or customers; here, too, it brings enforcement actions to challenge anticompetitive business conduct that injures farmers.

MERGER ENFORCEMENT

In our conversations with farm groups, we have found that farmers are especially concerned about the potential impact of mergers and acquisitions ("mergers"). Farmers are concerned that mergers will limit the number of sellers of seed, chemicals, machinery, and other equipment from whom they can buy and will limit the number of customers for crops and livestock to whom they can sell. For this reason, I think it may be helpful to start with a discussion of the Antitrust Division's merger enforcement program, with particular emphasis on recent merger enforcement actions that the Antitrust Division has taken in the agricultural sector.

MERGER ENFORCEMENT STANDARDS

Section 7 of the Clayton Act prohibits the acquisition of stock or assets if "the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly." This enables us to arrest anticompetitive mergers in their incipiency, to forestall harm that would otherwise ensue but be difficult to undo after the parties have consummated a merger. Thus, merger enforcement standards are forward-looking and, while the Antitrust Division often considers historic performance in an industry, the primary focus is to determine the likely competitive effects of a proposed merger in the future.

The Antitrust Division shares merger enforcement authority with the Federal Trade Commission ("FTC"), with the exception of certain industries in which the FTC's jurisdiction is limited by statute. The agencies jointly have developed Horizontal Merger Guidelines that describe the inquiry they follow in analyzing mergers. "The unifying theme of the Guidelines is that mergers should not be permitted to create or enhance market power or to facilitate its exercise. Market power to a seller is the ability profitably to maintain prices above competitive levels for a significant period of time." Merger Guidelines § 0.1.

We ordinarily seek to define the relevant markets in which the parties to a merger compete and then to determine whether the merger would be likely to lessen competition substantially in those markets. In performing this analysis, the Antitrust Division and the FTC consider both the post-merger market concentration and the increase in concentration resulting from the merger. Generally speaking, the Antitrust Division has been likely to challenge a transaction that results in a substantial increase in concentration in a market that is already highly concentrated, although appropriate consideration has also been given to other factors, such as the likelihood of entry by new competitors, that could affect whether the merger is likely to create or enhance market power or facilitate its exercise.

In most instances, the concern raised by a merger is the potential ability of the merging companies to raise above the competitive level the price of the products or services they sell. Of course, it is also possible that a merger will have the potential to substantially lessen competition with respect to the price that the merging companies pay to purchase products or services. This is a matter of particular concern to farmers, who often sell their products to large agribusinesses. The Merger Guidelines specifically provide that the same analytical framework used to analyze the "seller-side" is also applied to the "buyer-side": Market power also encompasses the ability of a single buyer (a "monopsonist"), a coordinating group of buyers, or a single buyer, not a monopsonist, to depress the price paid for a product to a level that

is below the competitive price and thereby depress output. The exercise of market power by buyers ("monopsony power") has adverse effects comparable to those associated with the exercise of market power by sellers. In order to assess potential monopsony concerns, the Agency will apply an analytical framework analogous to the framework of these Guidelines.

Merger Guidelines § 0.1. Thus, the Antitrust Division has reviewed mergers to determine not only whether they posed a competitive threat to persons buying goods or services from the merged entity, but also—as demonstrated by the Cargill/Continental case—whether they posed a competitive threat to persons selling goods or services to the merged entity.

While most of the merger challenges brought by the Antitrust Division have involved companies that compete with one another ("horizontal competitors"), the agencies also consider whether mergers involving companies at different levels in the production and marketing process ("vertical relationships") may have anticompetitive consequences. Challenges to vertical mergers are less frequent because these mergers often allow the merged companies to compete more efficiently in the marketplace, by reducing costs or streamlining production. However, there are circumstances in which a vertical merger may substantially lessen competition, such as by foreclosing competitive access to one of the markets involved in a way that raises barriers to entry or otherwise threatens competitive prices. In those instances, the Division takes whatever enforcement action may be warranted.

PROCEDURES FOR REVIEWING MERGERS

The Antitrust Division and the FTC use a clearance process to work out which agency will review a particular merger. The primary determinant is agency expertise about the product or service at issue, so that a merger is usually reviewed by whichever of the two agencies is most knowledgeable about the relevant product or service.

We take concentration into account from the beginning of our review. In determining whether or not to conduct an investigation, we consider the pre-merger and post-merger concentration levels in the affected markets. In those industries already characterized by high concentration levels, there is a substantially increased likelihood that a proposed merger is subjected to a formal—and often quite extensive—antitrust investigation.

The Antitrust Division and the FTC have an array of investigatory tools from which to choose in conducting such an investigation. Parties to most mergers meeting certain size thresholds must provide the agencies with advance notice and observe a waiting period before consummating the merger, during which time the reviewing antitrust agency may obtain relevant information and conduct an investigation. In circumstances in which such notice is not required, the reviewing antitrust agency has other statutory powers for obtaining information.

If the reviewing antitrust agency concludes that the merger is not competitively problematic, the investigation ends and the parties then are generally free to proceed with the merger. However, if the reviewing antitrust agency identifies competitive concerns, it explains the nature of those concerns to the parties, and the parties have an opportunity to address them. Unless the parties can convince the agency that its competitive concerns are not warranted, the agency prepares to file suit to seek an injunction against the merger.

Sometimes the parties make a proposal to address the competitive concerns that the reviewing antitrust agency has identified. For example, when a merger between multi-product firms raises competitive concerns with respect to only a subset of their products, divestiture of the competitively problematic product lines may solve the competitive problem, allowing the parties to proceed with the rest of the merger. There are times, however, when the merging parties' proposed changes to the merger are not enough to solve the problem or the problem is so pervasive that the agencies conclude the transaction must be prohibited in its entirety. In those circumstances, the reviewing antitrust agency challenges the merger in court, generally seeking a preliminary injunction to prevent consummation of the merger while it is being challenged.

RECENT MERGER ENFORCEMENT ACTIONS IN AGRICULTURE-RELATED INDUSTRIES

As a result of the clearance process with the FTC, the Antitrust Division has investigated the preponderance of mergers affecting agriculture, with a prominent exception being grocery store mergers, which are usually reviewed by the FTC. In the past few years, the Antitrust Division has successfully challenged four significant proposed mergers in agriculture-related industries that we concluded would adversely affect farmers. Each of those transactions was important in its own right,

and, collectively, they demonstrate the Division's commitment to enforce the antitrust laws in this vital segment of our economy.

Three years ago, the Antitrust Division investigated Monsanto's proposed acquisition of DeKalb Genetics Corporation. Both companies were leaders in corn seed biotechnology and owned patents that gave them control over important technology. We expressed strong concerns about how the merger would affect competition for seed and biotechnology innovation. To satisfy our concerns, Monsanto spun off to an independent research facility its claims to agrobacterium-mediated transformation technology, a recently developed technology used to introduce new traits, such as insect resistance, into corn seed. Monsanto also entered into binding commitments to license its Holden's corn germplasm to over 150 seed companies that currently buy it from Monsanto, so that they can use it to create their own corn hybrids.

Two years ago, the Antitrust Division comprehensively reviewed the proposed purchase by Cargill of Continental's grain business, which resulted in a suit to challenge the merger as originally proposed. The merger affected a number of markets. The parties were buyers of grain and soybeans in various local and regional domestic markets and also sellers of grain and soybeans in the United States and abroad. We carefully looked at all of the potentially affected markets, and ultimately concluded that the proposed merger likely would have anticompetitively depressed prices received by farmers for their grain and soybeans in certain regions of the country; we were also concerned that the merger would have had anticompetitive effects with respect to certain futures markets.

To resolve our competitive concerns, Cargill and Continental agreed to divest a number of facilities throughout the Midwest and in the West, as well as in the Texas Gulf. The nature of the relief demonstrates the individualized attention that we paid to local and regional markets. We insisted on divestitures in three different geographic markets where both Cargill and Continental operated competing port elevators: (1) Seattle, where their elevators competed to purchase corn and soybeans from farmers in portions of Minnesota, North Dakota, and South Dakota; (2) Stockton, California, where their elevators competed to purchase wheat and corn from farmers in central California; and (3) Beaumont, Texas, where their elevators competed to purchase soybeans and wheat from farmers in east Texas and western Louisiana.

We also required divestitures of river elevators on the Mississippi River in East Dubuque, Illinois, and Caruthersville, Missouri, and along the Illinois River between Morris and Chicago, where the merger would have otherwise harmed competition for the purchase of grain and soybeans from farmers in those areas. The Illinois River divestitures (and an additional required divestiture of a port elevator in Chicago) also prevented the merger from anticompetitively concentrating ownership of delivery points that have been authorized by the Chicago Board of Trade for settlement of corn and soybean futures contracts.

In addition, we required divestiture of a rail terminal in Troy, Ohio, and we prohibited Cargill from acquiring the rail terminal facility in Salina, Kansas, that had formerly been operated by Continental, and from acquiring the river elevator in Birds Point, Missouri, in which Continental until recently had held a minority interest, in order to protect competition for the purchase of grain and soybeans in those areas.

This relief was designed to ensure that farmers in the affected markets would continue to have alternative buyers for their grain and soybeans. After reviewing public comments on the proposed consent decree and the Division's response to those comments, the court determined that the decree was in the public interest and entered it in June 2000.

In November 1999, the Antitrust Division filed a complaint challenging the proposed merger between New Holland and Case Corporation because of our concern that the transaction would lead to higher prices for certain types of machinery purchased by farmers. The parties manufactured and sold two- and four-wheel drive tractors that were used by farmers for a variety of applications, including pulling implements to till soil and cultivate crops. They also manufactured and sold a variety of hay and forage equipment, including square balers and self-propelled windrowers. The Antitrust Division concluded that the transaction would significantly lessen competition and lead to higher prices and lower-quality products.

The parties agreed to significant divestitures in order to resolve our concerns. Those divestitures included New Holland's large two-wheel-drive agricultural tractor business, New Holland's four-wheel-drive tractor business, and Case's interest in a joint venture that makes hay and forage equipment. Following the public comment and response period, the court determined that the decree was in the public interest and entered it in March 2000.

Last year, Monsanto abandoned its proposed acquisition of Delta & Pine Land Co., after the Antitrust Division indicated that it was prepared to challenge the merger in court. The Division concluded that the merger, which would have combined the two largest cotton seed companies, would have anticompetitively harmed farmers raising cotton.

Taken as a whole, these enforcement actions provide a good picture of our merger enforcement efforts in agriculture-related industries. The Antitrust Division carefully reviews agricultural mergers for their competitive implications, and files suit if a merger is likely to lead to anticompetitive prices either for products purchased by farmers (New Holland/Case) or for products sold by farmers (Cargill/Continental). The Division's concerns are not limited to traditional agricultural products, but extend also to biotechnology innovation (Monsanto/DeKalb and Monsanto/Delta & Pine Land). And, while the Antitrust Division considers proposed divestitures and other forms of relief that permit a merger to proceed as restructured, the Division challenges a merger outright if it concludes that lesser forms of relief are not likely to address fully the competitive problems raised by the merger (Monsanto/Delta & Pine Land).

CRIMINAL ENFORCEMENT OF THE ANTITRUST LAWS

In addition to enforcing the antitrust laws against anticompetitive mergers, the Antitrust Division has moved aggressively to prosecute companies that engage in price fixing or allocation of markets or customers. Such conduct willfully subverts the operation of free markets and can cause serious economic harm. It virtually always results in inflated prices to purchasers or depressed prices to suppliers; indeed, that is the very purpose of such conduct.

Section 1 of the Sherman Act prohibits contracts, combinations, and conspiracies that restrain trade. The key to such illegal conduct is an anticompetitive agreement among competitors. It is not enough for the Antitrust Division to show that competitors charged the same or similar prices for a product or service. We must prove that the competitors agreed upon prices or price levels, or upon the allocation of customers or markets. A company convicted of violating the antitrust laws is subject to substantial fines, and an individual convicted of violating the antitrust laws is subject to substantial fines and imprisonment.

In the past few years, the Antitrust Division has prosecuted a number of cases and secured convictions and hefty fines in various industries involving products purchased by farmers. Two prosecutions deserve particular mention.

—Beginning in 1996, the Antitrust Division prosecuted Archer Daniels Midland and others for participating in an international cartel organized to suppress competition for lysine, an important livestock and poultry feed additive. The cartel had inflated the price of this important agricultural input by tens of millions of dollars during the course of the conspiracy. ADM pled guilty and was fined $100 million—at the time the largest criminal antitrust fine in history. Two Japanese and two Korean firms also were prosecuted for their participation in the worldwide lysine cartel and were assessed multi-million-dollar fines. In addition, three former ADM executives were convicted for their personal roles in the cartel; two of them have been sentenced to serve 36 and 33 months in prison, respectively, and fined $350,000 apiece for their involvement, and the other executive had 20 months added to a prison sentence he was already serving for another offense.

—Two years ago, the Antitrust Division prosecuted the Swiss pharmaceutical giant, F. Hoffmann-La Roche Ltd., and a German firm, BASF Aktiengesellschaft, for their roles in a decade-long worldwide conspiracy to fix prices and allocate sales volumes for vitamins used as food and animal feed additives and nutritional supplements. The vitamin conspiracy affected billions of dollars of U.S. commerce. Hoffman-La Roche and BASF pled guilty and were fined $500 million and $225 million, respectively. These are the largest and second-largest antitrust fines in history—in fact, the $500 million fine is the largest criminal fine ever imposed in any Justice Department proceeding under any statute. Three former Hoffmann-La Roche executives from Switzerland and three former BASF executives from Germany agreed to submit to U.S. jurisdiction, to plead guilty, to serve time in a U.S. prison, and to pay substantial fines for their role in the vitamin cartel. These prosecutions were part of an ongoing investigation of the worldwide vitamin industry, in which there have been 24 corporate and individual prosecutions to date, including convictions of Swiss, German, Canadian, Japanese, and U.S. firms, and convictions of 12 American and foreign executives who are serving or have served time in Federal prison, and another executive who has agreed to plead guilty and is awaiting sentencing.

The lysine and vitamin cases received substantial publicity because of the prominence of the companies involved, the amount of commerce at stake, and the record size of the fines. But we have also brought prosecutions on a smaller scale. We successfully prosecuted two cattle buyers in Nebraska a few years ago for bid-rigging in connection with procurement of cattle for a meat packer, after an investigation conducted with valuable assistance from the Department of Agriculture ("USDA"), which was investigating some of the same conduct under the Packers and Stockyards Act. In short, we have brought charges against companies that engage in criminal anticompetitive behavior that adversely affects farmers, from isolated acts to multi-year international conspiracies.

INVESTIGATIONS OF OTHER POTENTIAL ANTICOMPETITIVE CONDUCT

The Antitrust Division also investigates other forms of business behavior that may have anticompetitive effects. Such conduct may constitute an illegal restraint of trade under Section 1 of the Sherman Act or unlawful monopolization or attempted monopolization under Section 2 of the Sherman Act. Conduct that may raise competitive issues of particular interest to farmers include strategic alliances between agribusiness companies, joint ventures among suppliers, and restrictions imposed on intellectual property rights.

The Antitrust Division has conducted a number of civil investigations into whether some particular conduct is unreasonably restraining trade to the detriment of farmers. One such investigation resulted in the Division filing a lawsuit last fall to challenge a non-compete agreement between developers of long-shelf-life-tomato seeds, after we had concluded that the agreement was interfering with the development of new seeds for use by American farmers. That case is pending before the district court in Arizona.

OTHER AGRICULTURE-RELATED ACTIVITIES AT THE ANTITRUST DIVISION

The Antitrust Division has a long-standing cooperative relationship with USDA, through which we have provided assistance to each other in a number of respects. Division attorneys and economists investigating particular mergers have made extensive use of the wealth of information about agricultural markets that USDA collects in the ordinary course of its work. USDA has also contacted the Division to provide other useful information regarding major agriculture-related mergers we were investigating, and has forwarded investigative leads to the Division, such as the one resulting in the prosecution of the two cattle buyers in Nebraska for price-fixing. The Division has assisted USDA by consulting on studies USDA has conducted regarding competition-related aspects of agricultural markets, such as the red meat studies a few years ago, as well as on USDA's recent efforts to revise its investigative processes at the Grain Inspection, Packers and Stockyards Administration.

Two years ago, the Division entered into a memorandum of understanding with USDA, along with the FTC, to memorialize this working relationship and to reaffirm our commitment to work together and exchange information as appropriate on competitive developments in the agricultural marketplace.

The Antitrust Division also works with other relevant Federal agencies on specific matters of common interest. For example, the Division worked closely with the Commodities Futures Trading Commission during the investigation of the Cargill/Continental merger.

Last year, the Division created the position of special counsel for agriculture. The special counsel reports directly to the Assistant Attorney General and works exclusively on agricultural issues. The Antitrust Division has a full contingent of attorneys and economists available to work on agriculture-related matters, some of whom have extensive experience and expertise in those markets, and the special counsel has been a valuable complement to those existing enforcement resources, providing a sustained focus and public presence to our investigative and outreach efforts in agriculture. He has met with and spoken to a number of agricultural producers and producer groups, both here in Washington and in farm states, to explain to them how the antitrust laws work and how to bring relevant information to our attention. He has also met and maintained contact with a number of state attorneys general from farm states.

CONCLUSION

Mr. Chairman and members of the Subcommittee, we in the Antitrust Division understand the concerns that have been expressed about competition in agricultural markets. We take seriously our responsibility to ensure that the antitrust laws are

enforced no less vigorously in agricultural markets than they are elsewhere in our economy. We believe that our enforcement record demonstrates that commitment.

I would be happy to respond to whatever questions the Subcommittee may have.

Senator COCHRAN. Thank you very much, Mr. Nannes, for that overview of the Antitrust Division's role in this subject.

MANDATORY PRICE REPORTING

Ms. Waterfield, some are concerned that the mandatory price reporting system that was implemented this past April has had the effect of providing less information to producers than they received under the old voluntary system. Is this an accurate assessment? Or if it isn't, tell us what you think the benefits have been, if any, from the mandatory price reporting system.

Ms. WATERFIELD. Well, Senator Cochran, the mandatory price reporting system is legislation that is being handled, as you know, by our sister agency, the Agricultural Marketing Service. Obviously it affects the industries that we regulate and monitor.

We currently have two rapid response teams out, both in the cattle industry and the hog industry, talking with producers to ensure that there are no problems in the industries that we monitor as a result of mandatory price reporting.

What we found so far in the cattle industry is that there has not been much of an adverse impact as a result of mandatory price reporting.

ANTITRUST ENFORCEMENT

Senator COCHRAN. There has been some legislation proposed that would create some additional antitrust enforcement authority outside the Department of Justice at the USDA to oppose pre-merger review opinions.

My question is do you believe that creating a special counsel for competition within USDA who would have the same power as the assistant attorney general for antitrust at the Department of Justice would help in enforcement of agribusiness merger violations?

Ms. WATERFIELD. Is that directed at me, Senator Cochran?

Senator COCHRAN. Yes.

Ms. WATERFIELD. That question would be better addressed to the department's legislative affairs office.

Senator COCHRAN. Okay. Senator Dorgan had actually asked that we convene this hearing, and we discussed the logistics and where the hearing ought to be conducted and witnesses we ought to invite. And Senator Dorgan had another commitment, had to open a hearing at another appropriations subcommittee and therefore was not here for opening statements.

I'm going to yield at this time to Senator Dorgan for any opening statement that he would like to make.

STATEMENT OF SENATOR BYRON L. DORGAN

Senator DORGAN. Mr. Chairman, thank you. I will be brief, and I was at the Treasury appropriations subcommittee with Senator Campbell that we had to open up, and I apologize for being a bit late. Thank you for your statements. I read the statements of this panel and others.

If I might just use a couple of charts to make a couple of points, I'll be quite brief. Market concentration in the meat processing industry, the red line, is where we are now. Beef, 80 percent top four firms. Pork, 57 percent. Sheep, 73 percent. Poultry, 55 percent.

If I had put that chart up 20 or 30 years ago, it would have looked dramatically different than this, but this shows a level of concentration in those industries. Why do ranchers in my part of the country keep talking about concentration and the danger it involves for them?

Well, this chart shows 76 percent of the cattle market. 76 percent of the cattle market are under contract by the Big Four companies. Four percent bought on the public market by the Big Four. So when we talk about market share, the Big Four, and what it is doing to cattle market, and prices and so on, this is why ranchers are very concerned and becoming increasingly concerned as time goes on.

Let me just show two additional charts. Market concentration in the grain processing industry. Flour milling, top four firms, 62 percent. Wet corn milling, 74 percent. Soybean crushing, 64 percent.

Finally, let me show the charts of the farmer's share of the retail dollar, which interestingly enough moves in an inverse relationship to the concentration in the various industries. Farmer's share of the retail beef dollar is dramatically different, dramatically reduced. The farmers' share of the retail pork dollar exactly the same thing. The farmer's share of the cereal grains dollars, exactly the same thing.

The point is fairly obvious to me. As the enterprises in which farmers purchase from and the enterprises in the industries to which farmers sell become larger and have more economic muscle, they are reducing the farmer's share of the food dollar and increasing their own share.

And so our family farmers say is this a stacked deck? Is this a fair economy for us to operate in, or is there concentration here that is unhealthy? And I think the answer, from my standpoint, is there is concentration that is unhealthy.

I'm not an attorney who's schooled, for example, in antitrust law, but as I listen to the discussion here, it seems to me family farmers and ranchers in this country know that something is wrong. We are moving in the wrong direction, and somehow nobody seems to do much about it.

If I might just make a point, Ms. Waterfield said things have been fairly stable since 1995. I think that was her statement. In the pork industry, the four top pork producers in 1995, I believe, have become two pork producers through two major acquisitions. So changes are occurring even as we speak. This is moving very rapidly.

PREPARED STATEMENT

And the question is do we have a competitive market? And as soon as I have the opportunity to ask questions, Mr. Chairman, I'm going to ask questions. Do you think that the markets in these areas are more competitive or less competitive? So we can talk through that just a bit.

If they are, in fact, becoming less and less competitive and I would expect you would agree that is the case, then what are the remedies for that?

Mr. Chairman, you are kind to call on me for a statement, and I appreciate it.

[The statement follows:]

PREPARED STATEMENT OF SENATOR BYRON L. DORGAN

Mr. Chairman, I'd first like to thank you for holding this hearing on Market Concentration in agriculture. I requested that the Subcommittee hold this hearing, and I appreciate all of the work that you and your staff put into making it happen. Concentration in agriculture has been a growing problem for years. But now, it's quite obvious to most that the trend towards larger and fewer companies in control of our major agriculture markets is accelerating. I'm hopeful this hearing will help Congress find a solution to this ever pressing problem, and I commend you for your support on this issue.

I'd also like to welcome the diverse panel of witnesses appearing today. I say diverse, because we have with us today Federal agency heads representing the Department of Agriculture and Justice, state and university officials, livestock groups, farm groups, industry representatives, and a farmer. I look forward to hearing your views and any recommendations you may offer Congress in regards to legislative action aimed towards controlling the growth of agriculture market concentration.

During debate on the Packers and Stockyards Act of 1921, Wyoming Senator John B. Kendrick said, "The livestock industry has been brought to such a high degree of concentration that it is dominated by a few men. The big packers, so called, stand between hundreds of thousands of producers on one hand and millions of consumers on the other. They have their fingers on the pulse of both the producing and consuming markets and are in such a position of strategic advantage they have unrestrained power to manipulate both markets to their own advantage and to the disadvantage of over 99 percent of the people of the country. Such power is too great, Mr. President, to repose in the hands of any men."

Well, the Packers and Stockyards Act was passed. However, I believe Senator Kendrick's words would ring true again today. The numbers speak for themselves. The degree to which a few control these markets is astounding. Worse yet, the degree of concentration is increasing at a pace that causes compiled statistics to become obsolete soon after a study is completed. For instance, the top four pork producers of a couple of years ago are now just two Smithfield has devoured Murphy Farms and Carroll's Foods.

To survive and be assured of some stability due to slumping markets, farmers have increasingly turned to contract production. However, one look at the plight of many poultry producers and segment of agriculture which is almost exclusively controlled by contract production should cause many to pause if they consider contract agriculture the means to their salvation. I won't go into detail, but let me just say that it's common knowledge that the "first" contract offered a farmer is more than likely going to be the best. We've all heard about the poultry producers who are offered unfavorable contracts with a take-it-or-leave-it now ultimatum attached.

Almost every farmer out in the country cites growing market concentration and all the associated ills this plague produces as a serious problem that needs to be addressed. But, it isn't being addressed. Obviously, something is wrong. Either our anti-trust laws are not being enforced, or they need to be changed. Hopefully this hearing will deduce what exactly the problem is and then offer up a course of action to pursue to correct that problem.

Mr. Chairman, I want to thank you again for scheduling this hearing.

Senator COCHRAN. Thank you very much, Senator.

MARKET CONCENTRATION'S EFFECT ON ECONOMIC GROWTH

Mr. Collins, in your testimony, you raise the issue of market concentration and its affect on economic growth that usually results in a more efficient and higher quality product. Do you feel there has been a significant decline in research and development to enhance products due to market concentration? Or is it just the opposite?

Mr. COLLINS. Mr. Chairman, I think that is an issue that can cut both ways. I think in a highly concentrated industry where a firm may have market power, they may not necessarily need to do research and product development, innovate as much to maintain their market share. So that would be a force working against research and development.

On the other hand, as firms have gotten larger, they get deeper pockets, and they have more money available to conduct research and product development. I'm not exactly sure where that comes out. It would be something that you'd have to look at industry by industry.

We could look at the food products that are delivered to the American consumer today generally coming from the concentrated industries that Mr. Dorgan just identified all across the food processing and retailing. And yet we know that the food industry has been highly innovative and have done a lot to develop new products. I'll give you an example.

Back in the early 1970s, the food industry was producing about 1,000 new products a year. By the time we got to the mid 1990s, the food industry was introducing something in the order of 15,000 to 16,000 new products a year. That doesn't prove the point one way or another, but it does seem to me that as the economy has grown, despite concentration, we have seen a lot of research and product development innovation.

ANTITRUST VS. FTC RESPONSIBILITIES

Senator COCHRAN. In addition, Mr. Nannes, to the work of the Department of Justice and the Department of Agriculture through the grain inspection, Packers and Stockyard Act, the Federal Trade Commission also has some responsibilities. Are there enough laws on the books now that give these agencies and departments the powers they need to police and enforce or prohibit anticompetitive activity?

Mr. NANNES. Senator, in response to your question, let me note that, as you indicated, we and the Federal Trade Commission share antitrust enforcement responsibility. We worked out a liaison agreement with the Federal Trade Commission so that industries don't face duplicative antitrust investigations.

For example, the Federal Trade Commission is the agency that over time has developed the expertise with respect to supermarkets and grocery stores. So, it is the agency that has brought enforcement actions in that particular field.

With respect to mergers, we apply the same statute, which is section 7 of the Clayton Act, to which I made reference earlier. This is the statute that applies generally throughout the industry and across industry lines as the appropriate demarcation as between mergers that may be pro-competitive and efficient, and those that run the risk of creating or enhancing market power of the kind that Dr. Collins has referred to.

Over time, sir, I think section 7 of the Clayton Act has served as a very good framework for us to separate the anticompetitive transactions from transactions that do not present competitive risks.

Senator COCHRAN. It seems to me that the wording of the act, as you referred to it in your statement, is very broad. It gives the regulators a great deal of leeway to make decisions and to bring actions and to challenge mergers.

Mr. NANNES. Sir, that is correct, with one important limiting factor. And that is that we are a law enforcement agency. The judgments we make as prosecutors we have to be able to back up in court.

And so our ability to apply the antitrust laws is informed very substantially by the courts' interpretations of those laws. Over the course of the past 30-plus years, we have developed at various times merger guidelines that indicate to industry and to public bodies the factors we take into account when we are doing our merger review. So that operates also to inform the kind of judgments we make in merger review.

Senator COCHRAN. Senator Kohl.

Senator KOHL. Thank you very much, Senator Cochran.

DAIRY COMPACTS

Mr. Collins, in your prepared statement you said that within the food processing industry, dairy processors led the number of mergers and acquisitions in recent years. Could you provide any insight into the effect that dairy compacts may have on the trend towards concentration within the dairy processing sector?

Mr. COLLINS. Mr. Kohl, the Northeast Interstate Dairy Compact is very similar—the way it operates is very similar to Federal, milk marketing orders. It sets a minimum price for class 1 milk use for fluid consumption, just like Federal orders do.

I don't know of any research that has linked the milk marketing orders system to changes in consolidation or concentration in dairy processing. So my first answer to your question would be that I don't know of any studies that show a link.

I would say, however, that if you look at some of the theoretical factors that drive consolidation, one of the things that we've seen is consolidation in some markets that have slow growth. We've seen where there has been economies of scale, firms get larger, merge, acquire to offset the slow growth of demand.

They've gotten bigger to grow their own company by increasing their market share.

So milk marketing orders, I think, do slow the consumption of fluid milk. Fluid milk has been a stagnant industry anyway. It has been competing with soft drinks and fruit juices and all kinds of beverages. And when you raise the price of fluid milk that much higher, it slows consumption that much more.

Only to the extent that we've seen in some slow growth markets an incentive for firms to consolidate, I would argue that would be a link to the compact. But I would say it would probably be a fairly marginal, fairly small effect.

EFFECT OF GOVERNMENT PROGRAMS ON AGRICULTURAL CONSOLIDATION

Senator KOHL. Thank you, Mr. Collins. You mentioned government programs can contribute to agricultural consolidation, and concentration in a number of ways. Please identify these programs

most likely to increase or decrease concentration in the ag sector, especially those that are funded by this subcommittee.

Mr. COLLINS. That statement in my written testimony, Mr. Kohl, was not to suggest that the subcommittee is funding programs that spur consolidation. It was a general statement to say that government programs, tax policy, and regulation can encourage consolidation.

I think that some examples might be when we used to have passive loss investing which encouraged investment in feed lots, which led to consolidation in the feed lot business. I think you know things like patent laws, for example, do confirm a monopoly in the short term for firms.

It was just a general statement to say that government programs can contribute, as well as all the other factors I mentioned. I didn't mention that part in my opening statement. I mentioned all the other factors because I think the others have been more important, but government programs can be a factor as well.

I think farm program payments are an example. They cut both ways. We see farm program payments have raised agricultural land values, that is a barrier to entry for beginning farmers into agriculture or farm production. Payments going to large producers may, in fact, help them provide the financial leverage to buy out smaller producers.

It's a general statement that I think there are a lot of programs that do affect the pace of consolidation. And it's just something that we have to be mindful of when we implement programs and pass laws.

Senator KOHL. I thank you, Mr. Collins. I thank you, Mr. Chairman.

Senator COCHRAN. Senator Johnson.

Senator JOHNSON. Thank you, Mr. Chairman.

MANDATORY PRICE REPORTING

Two years ago, Mr. Collins, Congress adopted a mandatory price reporting legislation following passage in numerous States of State-based price reporting laws. Now that USDA has this legislation up and running, some livestock producers have expressed concerns about the so-called 360 guideline.

The 360 guideline prohibits the publication of a markets pricing information in any reporting period unless there are at least three firms reporting information for that market, and no firm has more than 60 percent of the trade for that market.

Producers have expressed concern to many of us that this will prohibit the reporting of pricing data on a daily basis if a firm with sizable concentration in an area of market is the only firm buying livestock.

I recognize the type of confidentiality at work here may be necessary to ensure proprietary business information not being inappropriately reported, and at the very least, the problem shed some light on the anticompetitive nature of the slaughter livestock market as a result of meat packer concentration, a larger issue that price reporting was never really intended to combat.

I know that USDA is aware of the 360 problem and is examining some alternatives, and I also believe it is only fair to give USDA

some time to implement price reporting. And at this stage, the 360 rule I don't think should be seen as a death knell of price reporting.

But if this problem grows and other problems spring up that lead to less and untimely market information, then Congress may need to take legislative action.

I believe it's in our mutual interest to ensure producers have confidence in the rules and guidelines used to implement the price reporting law. And so the questions I have for you, first, does USDA have the authority to make adjustments to the 360 rule without new legislation, would it be helpful to back up any price reporting changes with some sort of cleanup effort on our part?

Second, any updates you have on the implementation and, lastly, are additional funds needed in order to make this program work?

Mr. COLLINS. Mr. Johnson, I would be happy to answer this question as best I can. It's a similar question Mr. Cochran asked Ms. Waterfield, I believe. I would like to step back and just comment on this for a minute.

This is a story of good news, bad news, and hopefully good news in the end. Certainly it is a story of some frustration at the Department of Agriculture.

I know members on this committee like Mr. Dorgan, like yourself were instrumental in supporting mandatory livestock reporting which resulted in legislation in 1999. And on April 2nd we put into effect mandatory livestock reporting.

The good news about that is that an area of the farm economy that needed more information has legislation and a means now to get more information to help improve the competitive bargaining power of producers.

We put out under mandatory price reporting what we call 91 reports, 91 data series; 41 of those are new and have never been reported before. A lot of that has to do with forward contracted sales and that sort of thing.

The good news is we've got a system up, it was put in place April 2nd, and it's going to provide and it is providing more information than we have provided before.

The bad news is there have been some glitches. The first glitch has been what we're calling technical difficulties. And there are two forms of technical difficulties.

One form is software problems. We have a contractor that has developed the software. Sometimes the software has not aggregated the data right, so we haven't reported a data point on some days. At other times, the data that are reported, if you've looked at any of these reports as I have, is hard to read. You don't know what you're looking at sometimes when you look at the data. So the reporting formats were not that good initially.

Those problems are being addressed and fixed, by and large. We did have another problem I think yesterday or the day before with another software problem on a data series, but by and large such errors happened mostly during the first week and a half of April.

I think we're now down to the point where out of the 91 reports only like 3 or 4 are not being reported because of technical difficulty. And I think within another week we're going to have those resolved.

3/60 RULE

The second source of problems that you identified has been the confidentiality issue. And it has been widely publicized that we have used this 3/60 rule to determine whether we're going to report data on a particular day, particular time of the day, such as 11:00 a.m. or 3:00 p.m. That 3/60 rule is one that we've used elsewhere in the department.

The National Agricultural Statistics Service uses a similar rule, having to require at least three entities to report with each having no more than some share of the market. We use a 60 percent share, other Federal agencies have used 50 percent or 70 percent. It's a standard rule for determining confidentiality.

The problem has been, of course, now if you look at our reports, particularly for direct cattle purchases in certain States, cash market cattle purchases in Texas, Oklahoma, in Kansas, in Nebraska, we haven't been reporting because of confidentiality. These were data we were reporting under the voluntary reporting system, and this has led to a lot of frustration by producers.

I can tell you the answer your question specifically, you asked if the 3/60 rule to change that would require legislation, the answer to that is no, it would not require legislation. It was not in the statute, it was not in the legislation. It's a reporting standard that we adopted diligently.

Secretary Veneman has been involved on this and has met on this issue. We're looking at alternative ways to approach this question, and I don't know that I can go into that in much detail.

There's some statistical formulaic ways you can use to see the maximum amount of information without identifying somebody.

There's alternative ways of looking at the market in deciding whether we're going to disclose the identity of a buyer or seller based on the information that's being reported.

It's a little more complicated than I first thought. As the statisticians have looked at it, I can tell you that we do have a couple of options identified and they are in the review and decision process right now.

And I think if we can get an agreement on doing something other than what we've been doing, I think we can rectify a lot of the problems that we're seeing with lack of reporting due to confidentiality.

If we don't get an agreement, if the people who are reviewing this stuff like our lawyers and others say no, we can't do this, then the only alternative is the second part of your question, do we need legislation? Yeah, that may be what it comes down to. We might have to revert to voluntary reporting for some series if there's no other way to get them.

Under voluntary reporting, the people that are reporting wanted that information public, they didn't care about disclosure. We could go back and do that again for the series that we can't get the adequate information on.

But I think you also said something important that you need to give the department a little time to work this out, and I appreciate you saying that. Because I think—the way I'm looking at it the moment sitting here today, I think we can do something here. Maybe

tomorrow that will be a different story, but today I think we can go do something here.

So with a little more time, hopefully we can start providing most of the 91 reports we're supposed to be providing.

Mr. JOHNSON. Well, thank you, Dr. Collins. And I do realize that this is complex, more complex than might first meet the eye to a casual observer. And it does take time to work it through.

On the other hand, we also want to urge you to be very expeditious in trying to get this work at the kind of level that it needs to work with.

Mr. COLLINS. It is a problem, Mr. Johnson, because there are producers who have priced for a long time their animals off of a base price. Now all of a sudden we're not reporting that base price, and they have to make an adjustment.

That causes a lot of concern that they might be taken advantage of. So we understand that, and we are working on this very diligently. We have a big meeting planned on it tomorrow.

Senator JOHNSON. Very good. If I may, Mr. Chairman, may I ask one additional brief question?

Senator COCHRAN. If it suits Senator Dorgan.

Senator JOHNSON. I should yield to Senator Dorgan.

SPECIAL COUNSEL FOR AGRICULTURE

Let me ask Mr. Nannes just very briefly, Senators Harkin and Lugar and I worked on legislation last year to create a special counsel for agricultural position in the DOJ's Antitrust Division.

Subsequent to our introduction of that legislation, Attorney General Reno created the position without our bill. And appointed Mr. Doug Ross to serve in that capacity. Once again this year, Senators Harkin, Lugar, and I are looking at this legislation.

Can you shed any light on whether Attorney General Ashcroft plans to have Mr. Ross continue in that role, or, if not, whether a new special counsel for agriculture will be appointed?

Mr. NANNES. I'll try, Senator. Senator, it's my recollection that the decision to appoint a Special Counsel for Agriculture in the Antitrust Division last year was actually made by the Assistant Attorney General.

I have not spoken specifically with Charles James about what his thoughts are with respect to a special counsel, and that decision would ultimately rest with him. I do know, as a general matter, that he is sensitive and understands the issues associated with the appropriate enforcement of the antitrust laws in agricultural industries. So it would be my expectation that he would turn to that matter quite promptly upon his confirmation.

Senator JOHNSON. I would appreciate it if you would convey to Mr. James the strong interest I have and I know numerous others have that there be a special focus on this effort within DOJ. And it's my hope that some special counsel will be appointed. I yield.

Senator COCHRAN. Senator Dorgan.

Senator DORGAN. Mr. Chairman, thank you. Some, myself included, are concerned that we have kind of a slow motion bureaucracy in dealing these issues of concentration, and family farmers get very impatient. I'd like to ask a couple of questions about these markets.

LESS COMPETITION VS. INCREASED CONCENTRATION

We have the Sherman Act, we have the Clayton Act. You, Mr. Nannes, talked about section 7 of the Clayton Act. Both Sherman and Clayton have been interpreted differently over a century, and sometimes used aggressively, sometimes not used at all.

Is it generally agreed by the three of you that there is less competition and more concentration in the following areas—these are markets that family farmers must purchase from—fertilizer, petroleum, seed, farm equipment. Would you generally agree that there is more concentration in those areas? And if there was more concentration, would you then conclude there is less competition in those areas?

Mr. COLLINS. I will start. I would agree there is more concentration. I think the question as to whether there is less competition, you'd have to go market by market, and I may not be fully informed on all of them. But I would say that is a much more difficult question.

Within the economics profession, for example, in meat packing, I would say there is no consensus. The body of literature shows some studies would argue that there is the exercise of market power, that we're not getting competitive pricing. Other studies would argue that we are getting competitive pricing.

The seed industry is almost another example on its own because the seed industry is complicated not only by concentration but it is complicated by very far-reaching patent protection. So there are these reach-through-the-chain kinds of patent protection which confer some market power on firms that have such patents.

Senator DORGAN. Would you agree the loss of the share of the food dollar that farmers are suffering? You saw the charts I used. I would assume you would agree with the direction of the charts, that you could logically conclude that the loss of the farmer's share of the food dollar relates to the concentration of those they sell to and buy from.

Mr. COLLINS. No, I don't think I could.

Senator DORGAN. Then let me ask it a different way. You talked about markets that farmers sell into, pork, beef, grain trade, and so on. Is there general agreement that there has been substantial increased concentration in those areas?

Mr. COLLINS. Yes, I agree there has been.

Senator DORGAN. Do you generally agree, to the extent we teach things in economics that stand the test of time, that when you have more concentration that competition travels in an inverse relationship to concentration?

Mr. COLLINS. Not necessarily. I think you certainly can have increased concentration, but you can still have a perfectly competitive outcome in industries, even though they continue to concentrate.

Beyond some point, and there's no hard and fast rules about this, I know there are merger guidelines, for example, the Department of Justice would use, beyond some point they raise a lot of flags.

You get so few firms that have such high market share that then the prospect, the probability of anticompetitive pricing arises. But whether it actually occurs or not requires you to go in and look at the competitive behavior of the individual firms. You certainly

could have low barriers to entry. You certainly could have substitute products that are not in that industry that could constrain price, the exercise of market power and constrain excess pricing.

Senator DORGAN. Could you have purchase competition with two competitors in every one of these industries I've described under your analysis ?

Mr. COLLINS. Theoretically, yes, but I doubt it. Unlikely.

Senator DORGAN. Is it more unlikely that you have purchase competition or near purchase competition if you have 4 competitors controlling 80 percent of the industry versus 10 competitors 20 years ago or 30 competitors 50 years ago?

Mr. COLLINS. I would say that as a probability statement, yes, the probability is that you would have less competitive pricing in the more highly concentrated market.

But my problem with saying that with probability one is the lack of the empirical literature to support it.

FOOD DOLLAR TRENDS TO FAMILY FARM

Senator DORGAN. Let me try one more time for just a moment on this issue of the shrinking percentage of the food dollar that is achieved by family farms in this country. To what would you attribute that trend, if it is not to concentration in the industries that farmers buy from and sell to? What other conceivable reason would exist for that?

Mr. COLLINS. I'll take a shot at that. I haven't looked at that trend for all time, but I have looked at it since the 1950s. The farm share of the consumer dollar and, by the data we report, is the value at the farm level of the farm production that goes into the products bought by consumers—consumer expenditure for both food at home and food away from home.

So in 1952 the farm share of that consumer expenditure dollar was 42 percent. In 1999, it was 20 percent. So it clearly has gone down, and it's gone down as industries have concentrated.

The problem with drawing causation effect is there is a lot of other things have happened too. Over the last 50 years, we've seen dramatic changes in the structure of our economy. We've seen women enter the work force. We've seen the demand for convenience foods. We've seen the movement to eat food away from home. We've seen the development of microwave ovens and microwavable food.

INCREASED MARKETING COSTS

Mr. COLLINS. What we've seen is a tremendous increase in the marketing costs that go into the retail price. And those marketing costs are coming because the food that is sold today is not the same food that was sold in 1950. It has a whole bunch of services and characteristics associated it with it that have changed over time to make it fresher, to make more convenient, and to make it different.

I mentioned the statistic earlier that we were having 1,000 new food introductions in 1970, and we had 16,000 new food introductions in mid 1990s, and there was also research and development costs associated with all of these food introductions.

Senator DORGAN. How many different companies, Mr. Collins?

Mr. COLLINS. I'm sure it is a much fewer number of companies.

Senator DORGAN. How many companies do you think market grains of the cereals at the grocery stores?

Mr. COLLINS. My guess is the four firm concentration ratio is about 85 percent.

Senator DORGAN. There's a lot of different products, aren't there?

Mr. COLLINS. There's a lot of different products.

Senator DORGAN. Highly concentrated on the grocery store shelf.

Mr. COLLINS. All of those different products add to the cost to the consumer through the research and development in bringing that kind of product to market.

Senator DORGAN. I understand and I appreciate your response. When I started economics, we also learned that you've got to have empirical data to sustain a conclusion. On the other hand, when you see cars drive at night with their lights on, one can conclude it's because it's dark out. And——

Mr. COLLINS. Based on statistics.

Senator DORGAN. Yeah. Let me ask one final question, if I might, of Mr. Nannes. I would like to submit a list of questions to the panel. I appreciate the testimony of the panel.

CLAYTON ACT

Mr. Nannes, do you think there is reason or need to take a look at changing section 7 of the Clayton Act in any way? I think your testimony suggested that you think it is working and perfectly usable. Do you see a need for change at this point?

Mr. NANNES. Senator, my personal view would be not to change section 7. The statute has been changed a couple of times over the years. What it forces people to do then is to substantially recalibrate the extent of permissible and impermissible transactions and makes business much less certain.

Right now we have a series of guidelines that have been published by the Federal agencies and have been out there in the marketplace for quite a while. I think they are appropriate in that they set certain benchmarks of concentration levels that prompt concern, but properly direct the agencies, once they're looking at a transaction, to try to assess as best we can the likely competitive effects of the transaction.

It would be difficult, I think, to change it without having very substantial ripple effects across the broad range of not only U.S. companies but also foreign companies that have to deal with our antitrust laws.

Senator DORGAN. Mr. Chairman, we have two other panels, and I appreciate the testimony of this panel. I must say in conclusion a whole lot of farmers and ranchers feel they are victims at this point to a marketplace that is not working to a marketplace that is highly concentrated both in which they sell their products and from which they buy their products.

They look to us to be the referees in determining what is competitive and anticompetitive behavior. And the purpose of holding this hearing is to plung the depths of some of these topics, and I appreciate your testimony today.

Senator COCHRAN. Thank you, Senator. We appreciate your being here. Thank you very much for your contribution to our hearing.

We will now call our second panel to the witness table, and I will introduce them as they are coming up to take their places.

Mark Dopp is Senior Vice President and General Counsel of the American Meat Institute. William Roenigk is the senior Vice President of the National Chicken Council. John Caspers is Vice President of the National Pork Producers Council. David Reiff is representing the National Grain and Feed Association. And Fred Stokes is president of the Organization for Competitive Markets.

We have copies of the statements that have been prepared by the members of this panel. We will print those statements in the record in full and encourage our witnesses to summarize their statements so we will have an opportunity to discuss the issues with you in our question period.

PREPARED STATEMENT

I might say also that Senator Durbin of Illinois was here at the beginning of this hearing and has an opening statement which we will file and make a part of the record in full.

[The statement follows:]

PREPARED STATEMENT OF SENATOR RICHARD J. DURBIN

Mr. Chairman, Senator Kohl, thank you for holding this important hearing today. First, I'd like to welcome David Reis (pronounced rice) to this morning's hearing. He will testify later today—on the third panel—about his experiences with a livestock cooperative in central and southern Illinois.

David is a fifth generation family farmer from Ste. Marie in Jasper County, Illinois and the president-elect of the Illinois Pork Producers Association.

I invited David to come to Washington and to testify today because of his active involvement in American Premium Foods Co-Op. Over a year ago, David led a group of pork producers to Capitol Hill to discuss ways to improve farm prices and the rural economy. He presented an innovative co-op concept that would ultimately benefit more than 240 independent Illinois pork producers and help stabilize a shaky rural economy.

Just a few years ago, our nation's pork producers had to struggle with historic low hog prices that put many producers out of business. Value-added ventures, such as American Premium Foods, will help small to medium-sized producers compete in the ever-changing pork industry by ensuring market access, reducing price risk, and generating greater net returns.

As you will hear from David, starting a new business isn't easy. David's story, determination, and common sense approach to marketing agricultural products are good examples of a farmer who is embracing modern, 21st Century solutions to old problems.

In addition to David Reis, I want to say a word of welcome to another Illinoisan, Dan Kelley. Dan is the Chairman of the Board of Growmark and is from Normal, Illinois. We all recognize Growmark as an example of a successful and well-established cooperative.

I believe it is a testament to the cooperative system that we have two Illinois representatives here today. Nationally, there are approximately 48,000 cooperatives generating more than $500 billion in annual economic activity. Although this concept of producers working together is not new, many farmers are finding innovative ways to come together in order to improve their position in the marketplace.

To help encourage the establishment of value-added cooperatives, I will be working with my colleague, Sen. Charles Grassley, to fully fund a Federal grant that helps cover start-up costs for these businesses. These grants are the only funding dedicated to value-added businesses. Unfortunately, as currently written, USDA's fiscal year 2002 budget does not include adequate funding to cover start-up costs for these co-ops.

Currently the Department has designated $10 million for a round of these value-added grants. This doesn't begin to cover the growing demand. More than 200 applications totaling at least $55 million were recently submitted by cooperatives from throughout the country.

As we look at ways to address concentration in agriculture, we should not forget that innovative cooperatives are a constructive answer to helping individual producers maintain competitiveness. User-owned, user-controlled, and user-benefitted cooperatives can help family farms survive and thrive.

Thank you, Mr. Chairman. I look forward to working with you and the Subcommittee to address the needs of our nation's cooperatives.

Senator COCHRAN. He also wanted me to extend a special welcome to Mr. David Reis, who is going to be a member of our third panel.

So let's begin with panel number 2. Mr. Dopp, you may proceed.

STATEMENT OF MARK D. DOPP, SENIOR VICE PRESIDENT AND GENERAL COUNSEL, AMERICAN MEAT INSTITUTE

Mr. DOPP. Thank you, Mr. Chairman, other members of the subcommittee. Since 1906, AMI has represented the nation's meat and poultry industry, which today employs nearly 500,000 individuals and contributes about $90 billion in sales to the nation's economy.

Along AMI's member companies, 60 percent are small family-owned businesses employing fewer than 100 persons. These companies operate in one of the toughest, most competitive, and certainly the most scrutinized sectors of the economy. In fact, adhering just last fall, a former USDA general counsel stated the meat industry is probably the most studied industry in the U.S. economy.

Food production, distribution, and marketing sector has undergone a phenomenal change in the past decade. Consumers demand a constant and geographically dispersed supply of consistent quality, low-priced products. This demand has driven consolidation in the retail sector and, in turn, food manufactures have consolidated in an effort to keep peace with the retail and food service customers.

We see similar trends in the healthcare, financial services, high tech, and other industries.

Tough competition in the meat industry is driving businesses to operate more efficiently and more aggressively than ever before. My member companies believe consolidation is a response to intense competition and marketplace realities. It is not part of some sinister plot.

Mr. Chairman, mergers and acquisitions are viewed by today's business and investment community as generally good developments because they help sustain or strengthen businesses, they reserve jobs, and often they keep communities financially healthy.

The fact is it is better for a struggling meat packer to merge or be acquired and stay in business than for that company to cease operations costing all of the employees their jobs.

This fact is especially true in smaller rural communities where meat packing company may be one of the community's larger employers. Against this economic backdrop, AMI opposed the various agribusiness antitrust bills that have been introduced in recent years. Bills that would create new and different pre-merger review processes and antitrust enforcement procedures for the agribusiness sector. Allow me to comment on a few specifics.

One idea would allow USDA to oppose the pre-merger review opinions of the Justice Department, thus pitting one Federal agency against another. This idea conflicts with the recent recommendation of the international competition policy advisory committee and

it would also give USDA access to pre-merger review documents containing extremely sensitive information about the affected companies.

Last year GAO issued a report highly critical of grain inspection Packers and Stockyards Administration. And given those criticisms, it seems ill advised to confer more authority on that agency.

Although the bills at issue are intended to save the rural Americans, we believe they will have the opposite affect. A merger or acquisition often is the only way to preserve a sales outlet or input supplier for America's farmers. And bills that seek to bar such mergers would have a chilling affect on the already financially ailing agribusiness sector.

Stalling mergers could impede the flow of capital investment to the agribusiness community and could drive struggling businesses to close their doors. This hurts not only the customers and the input suppliers of America's farmers, but those farmers as well.

Some bills also would affect contracting. Contracts are important to agribusiness and to farmers because they help provide stability for buyers and for sellers.

For example, a bank may be more likely to approve a loan to a farm with contracts for its commodities, thus helping to finance expansion and efficiency. Currently such contracts are already subject to a host of Federal and State statutes.

Legislation has been suggested that would set special requirements for contracts between farmers and agribusinesses and, in effect, would allow government officials to participate in the contracting process. This concerns us.

It is one thing to call for a fair and legal contract, it is quite another to impose unique and ambiguous standards on one class of business that stem from a fundamental lack of understanding.

In that regard, we commend USDA's agricultural marketing service recently for posting on its web site information for farmers and others about how to understand the growing trend in contracting. In fact, educational efforts are probably a far better solution than legislation in this case.

Also of concern is the impact these bills will have on trade. Exports are key to the growth and viability of the livestock and meat industry. But competition is fierce. For example, U.S. exporters struggling for a share of markets in the Far East face very difficult competition from Canadian, Australian, New Zealand, Danish, and Argentine meat packers.

To the extent that the U.S. government adopts policies that increase the regulatory burden on American meat producers and processors or impedes structural adjustments that promote efficiency, U.S. meats become more costly and less competitive in foreign markets, and we risk losing market share.

PREPARED STATEMENT

In conclusion, the meat industry is but one of numerous sectors in the agribusiness community that would be hurt by the bills at issue. I urge you not to single out the agribusiness community for a different approach to pre-merger reviews and antitrust enforcement. Thank you for the opportunity to appear today, and I'd be happy to answer any questions.

[The statement follows:]

PREPARED STATEMENT OF MARK D. DOPP

My name is Mark Dopp and I am senior vice president and general counsel of the American Meat Institute. AMI has provided service to the nation's meat and poultry industry—an industry that employs nearly 500,000 individuals and contributes about $90 billion in sales to the nation's economy—for more than 94 years.

Among AMI's member companies, 60 percent are small, family-owned businesses employing fewer than 100 individuals. These companies operate, compete, sometimes struggle and mostly thrive in what has become one of the toughest, most competitive and certainly the most scrutinized sectors of our economy: meat packing and processing. In fact, at a hearing just last fall, a former USDA General Counsel stated that the meat industry is probably the most studied industry in the U.S. economy. I believe my member companies, who have cooperated with USDA, the General Accounting Office and many other interest groups and academic researchers on numerous studies, would agree with that assessment.

The food production, distribution and marketing sector has undergone phenomenal change in the past decade. Consumers today demand a constant and geographically dispersed supply of consistent quality, low-priced products. This demand has driven consolidation in the retail sector. Whether it's Home Depot for handyman supplies or McDonalds for burgers or Safeway for groceries, the American consumer has driven and benefited from this retail consolidation. In turn, food manufacturers have consolidated in an effort to keep pace with their retail and foodservice customers. And many that supply goods or services to food manufacturers—such as farmers, equipment or ingredient suppliers—have also consolidated. We see the same trends in the healthcare, financial services, pharmaceutical, telecommunications, airline, banking, automobile manufacturing and high-tech industries.

My member companies would argue that consolidation is a reaction to intense competition and marketplace realities. It is not—as some have suggested—some sinister plot in and of itself. Tough competition in the meat industry is driving businesses to operate more efficiently and more aggressively than ever before. And sometimes, that competition has meant that businesses choose to merge or to acquire or to be acquired in order to stay in business.

Mr. Chairman, mergers and acquisitions are viewed by today's business and investment community as generally good developments, because they help sustain or strengthen businesses, they preserve jobs and many times they keep communities financially healthy. Let's face it—it is better for a struggling meatpacker to merge or be acquired, and stay in business, than for that company to cease operations and release all of its employees. This fact is especially true in smaller, rural communities, where a meatpacking company may be one of the community's larger employers.

Against this economic backdrop, AMI's Board of Directors strongly opposes the agribusiness antitrust bills that have been introduced in recent years that would create new and different premerger review processes and antitrust enforcement procedures for the agribusiness sector.

REENGINEERING ANTITRUST ENFORCEMENT

One concept that has been discussed would give USDA the ability to oppose the pre-merger review opinions of the Justice Department, thus pitting one Federal agency against another. This idea conflicts with the recent recommendation of the International Competition Policy Advisory Committee (antitrust experts appointed by the U.S. Department of Justice).

Such a process would add uncertainty to the application of antitrust statutes. It would also give USDA access to pre-merger review documents containing extremely sensitive information about the affected companies (known as Hart-Scott-Rodino filings). Sharing such proprietary information with yet another government agency may well jeopardize its confidentiality, damaging the affected companies, their shareholders and investors, as well as their suppliers and customers.

GAO last year issued a report highly critical of USDA's Grain Inspection/Packers and Stockyards Administration (GIPSA). Given those criticisms of GIPSA, I suggest that any efforts to confer greater authority or responsibilities to that agency are, if not ill advised, certainly ill timed.

Other bills have proposed even broader changes to antitrust enforcement, affecting not only agribusiness, but also agriculture-related businesses. Specifically, those bills would affect all businesses that process agricultural commodities, as well as those who do business with the agriculture sector. For example, it has been proposed that businesses as diverse as banks, textile manufacturers, food processors,

supermarkets, paper mills, tobacco companies, seed companies and farm machinery manufacturers to file separately with USDA (in addition to the USDOJ) for pre-merger review and approval. These businesses would be required to disclose highly confidential information about contractual relationships and business alliances with USDA each year.

UNINTENDED CONSEQUENCES

Although these types of bills are intended to assist rural Americans, we believe they will have quite the opposite effect. It is important to remember that a merger or acquisition often is the only way to preserve a sales outlet or an input supplier for America's farmers. We believe these bills will have a chilling effect on the already financially-ailing agribusiness sector by creating obstacles to mergers and requiring the sharing of proprietary business information. Stalling mergers will impede the flow of capital investment to the agribusiness community and may well drive struggling businesses to close their doors rather than wade through a new morass of complicated pre-merger approval processes. The customers and input-suppliers of America's farmers will be hurt, and this will hurt, not help, America's farmers.

MANDATING NEW TERMS FOR AGRIBUSINESS CONTRACTS

A growing number of transactions between agribusinesses and farmers involve contracts. Provisions in these contracts cover everything from the quality of the agricultural commodity to its method or date of delivery to its volume to its price. Contracts provide a degree of stability for both buyers and sellers. For example, banks may be more likely to approve loans to farmers who hold contracts for their commodities; thus farmers benefit from the financial security offered by contracts. Currently, contracts between agribusinesses and farmers are developed on a case-by-case basis, guided by the Uniform Commercial Code and applicable provisions of the Packers and Stockyards Act, the Perishable Agricultural Commodities Act and other Federal and State statutes. Legislation to create new requirements for contracts between farmers and agribusinesses will have significant, negative legal and business implications.

Within some states and here in the U.S. Senate, some are considering legislation that would set special new requirements for contracts between farmers and agribusinesses. In general, the bills would mandate all contracts between farmers and agribusinesses to include a "clear written disclosure statement" describing material risks of the contract to the farmer. They would also require that the disclosure statement meet a host of "readability requirements," such as "ten-point modern type, one-point leaded," being written in "clear and coherent language using words and grammar that are understandable by a person of average intelligence, education and experience within the industry" and the inclusion of a "mandatory cover page." The mandatory cover page must include this statement, "READ YOUR CONTRACT CAREFULLY. This cover sheet provides only a brief summary of your contract. This is not the contract and only the terms of the actual contract are legally binding. The contract itself sets forth, in detail, the rights and obligations of both you and the contractor or processor. IT IS THEREFORE IMPORTANT THAT YOU READ YOUR CONTRACT CAREFULLY."

Some of the state bills also provide for each state attorney general or other, suitable official to review agricultural contracts and certify that they meet the requirements of the law. In the Senate bill, the Secretary of Agriculture would have this responsibility. The bill would also void all provisions of any agricultural contract that are confidential. We have serious concerns about the ambiguous provisions of this kind of legislation. It is one thing to call for a fair and legal contract. It is quite different to impose unique and ambiguous standards for one class of business that frankly stem from a lack of understanding. USDA's Agricultural Marketing Service should be commended for recently posting on its website new information for farmers and others on how to understand the growing trend of contracting. In fact, educational efforts are probably a far better solution than legislation in this case.

THE IMPORTANCE OF INTERNATIONAL TRADE

Exports hold the key, in fact will be the primary engine, to the future growth and viability of the U.S. livestock and meat industry. Whether we like it, the long-term viability of the sector depends on our ability to compete in world markets. U.S. exporters struggling for a share of many of the promising, newly invigorated markets in the Far East are facing ferocious competition from Canadian, Australian, New Zealand, Danish and Argentine meat marketers. To the extent the U.S. government adopts policies that increase the regulatory burden on U.S. meat producers and

processors or impede structural adjustments that promote efficiency, U.S meats become more costly and less competitive in foreign markets and we risk losing all-important market share.

We should remain focused on the fact that we are participating—or attempting to participate—in a global marketplace. Misguided decisions, intended to benefit one segment of the industry, could easily backfire to the detriment of the entire industry if such actions have the ultimate effect of pricing our meat products out of international markets.

CONCLUSION

The meat industry is but one of numerous sectors in the agribusiness community that would be hurt by antitrust or contract reform bills of the type begin contemplated. In addition to AMI, these bills are opposed by organizations as diverse as the antitrust section of the American Bar Association, to the National Association of Manufacturers, the U.S. Chamber of Commerce, the Grocery Manufacturers of America, the Food Marketing Institute and virtually all food and commodity processing organizations. I urge you not to single out the agribusiness community for a different approach to premerger reviews and antitrust enforcement. Thank you for the opportunity to appear before you today.

Senator COCHRAN. Thank you. Mr. William Roenigk, Senior Vice President of the National Chicken Council. Mr. Roenigk, you may proceed.

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

Mr. ROENIGK. Good morning. Thank you, Mr. Chairman, Senator Dorgan, and the other committee members for the opportunity to present the National Chicken Council's comments regarding agricultural market concentration. I will summarize my written comments.

I am Bill Roenigk, Senior Vice President of the National Chicken Council. Our organization represents companies that produce, process, and market about 95 percent of the birds in the United States. Almost without exception, these firms are vertically integrated from the live bird to delivery of consumer-ready products to the market.

These companies contract with independent farmers to have them manage breeder hatchery supply flocks and grow flocks of broilers. This arrangement has been the standard business model for the U.S. broiler industry since the late 1950s.

Last year's production of broilers was 20 times the amount in 1950. We believe such an impressive record of consistent growth is a good evidence that the system is serving well consumer, contract growers, and broiler companies.

At the same time, we've experienced this expansive production, the broiler industry, like many other parts of agriculture and agribusiness, continue to move towards fewer but larger survivors. There are currently about 45 commercially-sized broiler companies.

As consolidation occurs, however, very few operating assets cease production. Also I'm not aware of contract growers having their operations disrupted by this trend towards consolidation. If we could use GIPSA's latest annual report as a gauge of performance, I believe if you review that, you will conclude, like I do, that the industry's record is excellent, especially for the larger, more established firms.

There are many factors and pressures driving the U.S. Poultry industry towards fewer but larger companies. Continued intense competition within our own business and with competing red meat

industry requires companies to have the financial resources to sustain operations during prolonged periods of less than satisfactory levels of financial returns. That means losses.

The customers in the food sectors, whether they are supermarkets, restaurants, institutional buyers of raw material are not only becoming fewer and larger but more and more these companies are emphasizing centralized purchasing of products such as chicken.

As intense as the domestic market is, I believe the international markets are just, if not more so, demanding of the suppliers to the global market. These companies must be of adequate size to provide significant quantities of products. Being able to accept certain levels of market risk in the international markets also tilts the chances for success towards larger firms.

The dynamics of globalization are changing world markets. Dr. Bruce Babcock with Iowa State University last month told the Senate Agriculture Committee that the real action for U.S. agriculture exports is no longer grain and oil seed commodities but rather value added further processed products such as poultry, red meat, and similar products.

The National Chicken Council believes with the right regulatory and legislative and economic environment, the U.S. Poultry industry can continue to build exports that will help strengthen U.S. agriculture and the general economy.

Last year our industry exported over 18 percent of our production. I believe within 5 years more than one out of four pounds of U.S. chicken will be exported.

Also last month Secretary of Agriculture, Ann Veneman, expressed views similar to Dr. Babcock's. She noted that the sectors or the links in a food chain are more interconnected than ever because we have changing consumer markets demanding increasingly challenging the traditional ways of doing business.

Technology in many areas is transforming world markets and global relationships. The United States, according to the secretary, must have agricultural producers who can rapidly respond to the changes in global markets and all involved should recognize the interdependencies of the links in the food chain.

PREPARED STATEMENT

I believe Dr. Babcock and Secretary Veneman are correct in their assessments. It is time for us all to work across the links in the food chain to grow the opportunities for all of us.

I appreciate the opportunity to share the National Chicken Council's views with the committee.

[The statement follows:]

PREPARED STATEMENT OF WILLIAM P. ROENIGK

Thank you, Chairman Cochran, Senator Kohl, and Committee Members for the opportunity to present the National Chicken Council's views and recommendations regarding the very important issue of agricultural market concentration. The National Chicken Council appreciates the Chairman's invitation to be part of this very vital discussion. I am William P. Roenigk, Senior Vice President of the National Chicken Council.

The National Chicken Council represents companies that produce and process about 95 percent of the young meat chickens (broilers) in the United States. These vertically-integrated firms contract with growers to raise the live birds for proc-

essing and contract with breeder farmers to supply fertile eggs for hatching. The system of production, processing and marketing is highly coordinated and operates using the just-in-time method. Given the relatively short time from day-old chick to market-ready chicken, it is critical that such a system be in place and that all parts of the system operate in concert.

VERTICAL INTEGRATION

During the 1950s and 1960s broiler production and processing evolved into the vertically-integrated industry structure that has been the standard business model for five decades. Last year more than 8 billion broilers weighing over 41.5 billion pounds, liveweight, were produced. This production level last year was 20 times the amount in 1950. Few, if any, agribusinesses can match this record of growth. Success for achieving this amazing growth is based on providing wholesome, high-quality food while making chicken a better food dollar value essentially year after year. We believe the system has well served consumers, growers, and processors.

Contract growers and processors are mutually dependent on each other. It is in neither party's interest to jeopardize the economic viability of the other party. Almost one-half of all contract broiler growers have grown for the same processor for at least ten years and an additional 25 percent have contracted with the same company for five to nine years. Many growers have requested the opportunity to build more growout housing so that they can expand their operations. Further, most processors have waiting lists of other farmers who wish to begin growing broilers. The stability and success of the contract system for broilers has been good for agriculture.

REGULATORY AUTHORITY

The contractual relationship between broiler growers and the broiler firms is regulated by USDA's Grain Inspection and Packers and Stockyards Administration's (GIPSA). Periodically, this relationship is reviewed by Congress. In 1987, the administrative enforcement authority (including civil money penalty authority) of GIPSA with respect to transactions involving live poultry and poultry products was fully and carefully considered by Congress. Congress declined to provide more authority to GIPSA for any violations of the Packers and Stockyards Act (P&S Act) other than those relating to prompt payment and the statutory trust for live poultry dealers. NCC is not aware of conditions that have changed or developments that have occurred since 1987 that would warrant Congress reversing its decision.

Also, at certain times GIPSA argues that it needs authority to proceed administratively against, and impose civil penalties on, poultry processors who violate the P&S Act's prohibition against unfair or deceptive practices. GIPSA says such authority is needed because it has this authority already for the red meat industry.

As previously noted, poultry is produced, processed, and marketed in a very coordinated, vertically-integrated system. This business model's structure is distinctly different than the methods used in many other agribusinesses. Because young meat chicken is produced, processed, and marketed in a distinctly different system and because the vertically-integrated firms have successful, on-going contractual relationships with their growers, it is unnecessary to burden business with additional government regulations.

In short, unlike the situation in the production systems that are not closely-linked from production to processing to markets, private actions for breach of contract under common law contract principles, as well as under statutory provisions protecting growers, are available to police relationships among poultry growers, dealers, and processors, thereby going a long way to ensure fair dealing for all. This legal point about contractual obligations is important, but often overlooked in the discussion of the broader issue of regulating contractual relationships.

GIPSA, together with other government agencies, has more than adequate authority to ensure fair dealing within the poultry industry. First, GIPSA has authority to issue cease and desist orders and levy civil penalties for violations of the P&S Act's protections regarding prompt payment and the statutory trust. Second, GIPSA may investigate and refer to the Department of Justice for enforcement in the Federal Courts other violations of the P&S Act involving live poultry (for example, weighing practices and contract compliance). Finally, the P&S Act gives the Federal Trade Commission jurisdiction over marketing practices involving poultry products. There exists ample oversight and authority for poultry.

Regarding broiler companies performance with respect to GIPSA regulations involving contract growers, the 2000 Annual Report of the Grain Inspection, Packers and Stockyards Administration report, we believe, gives the industry high marks. For example, GIPSA investigated during fiscal year 2000 the operations of 97 live

poultry dealers. Nearly 44 percent of these investigations were the result of complaints received from contract growers. GIPSA investigations are designed to determine whether the contract settlement terms of live poultry dealers throughout the United States are deceptive or unfair to the growers who grow poultry under these agreements. According to the annual report, one violation was found and the company resolved the issue through a consent agreement.

Regarding protection for contract growers to be assured they receive payments, there are safeguards. In February 1988, the P&S Act was amended to include a statutory trust provision similar to the packer trust giving payment protection to live poultry growers and sellers. Since the 1988 amendments, live poultry producers have been paid $7.5 million under the statutory trust provisions. It is important to note, however, that during the twelve years since 1988 tens of billions of dollars in contract payments have been made on a regular, steady basis whether the market for chicken was robust or less-than-robust. The poultry trust payouts reflect claims for unpaid purchases of all types of poultry, including broilers, turkeys, and spent fowl.

GIPSA in its annual report said "(i)t (trust payouts) primarily shows the failure of small regional firms that have ceased operations and failed to pay growers or poultry sellers. It does not accurately portray an economic trend for the industry as a whole but only reflects a sum of the failures of small marginal operations. The national firms are large, completely integrated operations that are relatively stable financially. Any changes that occur are the results of mergers or sales of the total operation and do not usually result in losses to poultry growers or sellers." In fiscal year 2000, one poultry trust complaint was received by GIPSA, resulting in over $250,000 in payments to live poultry producers, the agency noted. Given the experience since 1988, it can be reasonably concluded that the statutory trust provision for poultry works and does provide adequate protection.

CHANGING MARKETS

Although the U.S. poultry industry does not have the same degree of market concentration as certain other meat processing industries, it clearly is experiencing the same marketplace dynamics that are occurring in many, if not most, food sectors. Intense competition within the chicken business and within the competing meat complex requires companies who want to be survivors to more carefully and adroitly analyze the changing markets. Then, of course, the real challenge is to convert the results of the analysis into a successful marketing plan.

Market pressures to meet the requirements of large national food chains, whether supermarkets or foodservice, is one major factor driving chicken companies to expand through acquisitions, resulting in a continued trend toward industry consolidation. However, the pressure is not just domestic. International demands are also increasing the global pressures on U.S. chicken companies.

A recent statement to the Senate Agricultural Committee by Dr. Bruce A. Babcock/Center for Agricultural and Rural Development, Iowa State University summarized this situation. He told the Committee. . . . "(a) significant change that has taken place over the last 10 years is the greater integration of world agricultural markets. Increased integration means that agricultural commodities will flow more readily to markets that offer a price premium. From an economist's perspective this means less price variability across markets and less price variability within domestic markets. From agriculture's perspective, greater integration means more competition and a greater need to deliver products that the world's consumers want. A farm bill that gives U.S. agriculture the right incentives to deliver the kinds of food products overseas customers want will enhance the long-term health and competitiveness of the sector."

Dr. Babcock also explained the future success for U.S. agriculture is likely to be capturing the trend toward more exports of value-added products, such as poultry and other animal products, rather than traditional commodities. To meet anticipated strong world demand, U.S. poultry and livestock producers must be competitive with favorable costs and high-quality products. In his testimony, he expressed his conclusion as follows, "(c)onsider the economic changes that have taken place over the last 10 years. Ten years ago, program commodities broadly defined (grains, feeds cotton, oilseeds and oilseed products) accounted for 64 percent of the value of agricultural exports. In 2000, they accounted for 49 percent. We project they will account for even less in the future. The United States faces increased competition in bulk grain and oilseed export markets. Export demand for higher-value commodities, such as meat, processed foods, and fruit responds directly to increased per-cap-

ita income levels. Thus, continued world economic growth will result in relatively greater demand for U.S. exports of these higher-value commodities." [1]

The important point is that the United States must maintain and improve a regulatory, legislative, and economic environment that will permit agribusiness to create, connect, and grow to meet this world demand for animal agriculture products.

A similar conclusion was recently expressed by Secretary of Agriculture Ann M. Veneman when she spoke at a recent agribusiness forum. The Secretary explained that the changing and increasingly demanding global market for U.S. agriculture products is impacting the basics of American agriculture. Last month she said, "(s)eventy years later, it no longer makes sense to speak of the "farm economy" as if it exists in some kind of vacuum. Today we must look at the entire food chain. The various sectors of the food economy are more interconnected than they've ever been, and they grow more interconnected every day.

U.S. agriculture operates in a global, high-tech, consumer-driven environment. Capital and information flow instantly between buyer and seller. And changing consumer demands are challenging existing marketing institutions and traditional ways of doing business."

The Secretary noted that multinational companies source raw materials from all over the world, process them and then sell throughout the world. Increasingly, she added, the global marketplace is being driven by consumers who demand quality, safety, health, and convenience, and who grow ever-more affluent. These globally-oriented firms need to create and maintain flexible relationships, strategic partnerships, and other alliances across the old boundaries that used to separate producers from processors from retailers, the Secretary explained.

Transforming world markets, Secretary Veneman said, are the technological improvements in transportation, storage and food science. Information technology is also vastly improving efficiency in all links of the food chain. Biotechnology is generating new products that make farmers more productive and consumers healthier. Further, the Secretary said many links of the food chain have changed, and will continue to change. For the U.S. broiler industry as it works to meet the stepped-up demands of the marketplace, Secretary Veneman's analysis could not be more correct.

Although Secretary Veneman's focus was on agricultural policy her analysis and recommendations clearly apply to the policy issues involving agricultural market concentration. She summarized the current agricultural market situation by noting that "(a)n agricultural policy for the 21st century should be one that can respond to the rapidly changing structure of global markets. It should be one that recognizes the interdependencies of the food chain. The success of input suppliers, farmers, processors, distributors, retailers, and consumers all depend on one another. The best path to an agricultural policy under which each of these segments of the food industry can prosper is to have each segment come to the table and work together to design the next generation of agricultural policies." [2] We agree.

CONCLUSION

Today's and tomorrow's market forces compel U.S. agribusiness to work across the links in the food chain to grow the opportunities for all. It is not a time to legislate and regulate about how best to arrange the links in the food chain.

The National Chicken Council is pleased to have this opportunity to provide our input. We look forward to working with the Subcommittee and other interested groups to address the issue of agriculture market concentration in a thoughtful, productive way.

Senator COCHRAN. Thank you very much.

Mr. Caspers, welcome.

STATEMENT OF JON CASPERS, VICE PRESIDENT, NATIONAL PORK PRODUCERS COUNCIL

Mr. CASPERS. Thank you, Mr. Chairman and members. I am a pork producer from Swaledale, Iowa, and serve as Vice President of the National Pork Producers Council.

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[1] Bruce A. Babcock, Center for Agricultural and Rural Development, Iowa State University. Testimony Before The United States Senate Committee on Agriculture, Nutrition and Forestry, April 25, 2001.

[2] Ann M. Veneman, Secretary of Agriculture, The Sparks Companies 9th Annual Food & Agricultural Policy Conference, April 17, 2001, Washington, DC.

Today I'm representing America's pork producers, and I'm pleased to discuss with you what we believe is a growing critical need for Federal Government investment and action regarding agriculture concentration.

Agricultural concentration is a difficult and emotionally charged issue. Many producers are concerned about their ability to continue to compete and maintain market access in a hog market that is experiencing increasing levels of concentration.

We need your help and understanding the relevant issues in order to take appropriate actions to assure an efficient marketplace that accurately rewards producers while providing an abundant supply of affordable, safe, and nutritious pork.

The concentration in the pork packing sector is measured by the four firm concentration ratio or CR4, grew from 32 percent in 1985 to 56 percent in 1998. GIPSA's 2000 annual report shows a CR4 of 56 in 1999. And the eight firm concentration ratio now stands in excess of 75 percent.

While not guaranteeing—not a guarantee of non-competitive conduct that increases consumer prices and producer prices, these levels and their trends increase the possibility of such conduct and provide ample incentive for ongoing research and heightened vigilance.

The CR4 for the hog production segment has grown from negligible levels in the early 1980s to about 18 percent following the 1999 acquisition of Carroll's Foods and Murphy Family Farms by Smithfield and the 2000 purchase of Lundies by Premium Standard Farms.

Vertical integration of packers owning hogs has grown from an estimated 6.4 percent in 1994 to roughly 24 percent today. The recent efforts of Tyson Foods to buy IBP brought this topic back to the forefront. We'll also submit a research paper commissioned by NPPC as part of the official record for this hearing. I believe it provides valuable insight into the relevant economic issues that should be considered in cases of mergers, especially those that involve vertical integration as well.

In addition to increasing vertical integration, vertical coordination through marketing contracts is increasing rapidly. As recently as 1994, 71 percent of hogs were sold in the cash market and only 20 percent were sold using a formula price. In January 2001, 82.7 percent were purchased through some type of contractual marketing agreement and only 17.3 percent were cash market purchases.

This trend has reduced the size of the negotiated hog market substantially and caused many concerns about the efficiency and accuracy about today's price discovery process. These concerns become even more acute when one considers that the price is 17 percent of the hogs sold through cash market transactions, directly sets the price for the 54 percent of all hogs that are sold on formula price contracts.

Firms are getting larger and controlling larger market shares at every level of the pork industry, including production, packing, processing, and retailing.

There's no doubt that this increased concentration increases the possibility for non-competitive behavior. To that end, the Federal

Government must be diligent and aggressive in enforcing the Sherman Act, the Federal Trade Commission Act, the Clayton Act, and the Packers and Stockyards Act.

Attacking perceived agricultural concentration problems with a regulatory or judicial acts may not, however, be as beneficial as sharpening the acts with more knowledge about today's firms and systems and how they work.

In fiscal 1992, Congress appropriated $500,000 for USDA to conduct a study of concentration in the red meat packing industry. The vast majority of these funds were spent investigating the fed cattle and fed beef segments, which and are still among the most highly concentrated in agriculture.

Since that time, though, the pork industry has changed more rapidly and more dramatically than virtually any other ag sector. MPBC has repeatedly asked Congress to pay the same kind of attention to the knowledge and understanding level of the pork industry that it paid to the beef industry in 1992. I renew that request today.

Specifically MPBC emplores this committee to approve appropriations for the following research. First of all, the Department of Agriculture should fund studies on hog market structure and competitiveness issues within the pork industry. All lying present realities, future scenarios, and the implications for producers' economic well-being in our nations food supply.

These studies would be similar to those done in the early 1990s for beef. We estimate they would cost approximately $750,000.

Secondly, to establish a yardstick against which claims of price discrimination could be compared, the Department of Agriculture should fund a study of the factors that comprise economically justifiable price differentials, including factors such as volume, time of delivery, carcass specifications, et cetera.

Such research may involve detailed work on packing plant and packing firm economics, a portion of which MPBC has already initiated and would be willing to share with USDA researchers as part of a comprehensive research effort. We estimate this project could be completed for approximately $400,000.

Thirdly, a study of the threshold levels of standard concentration measures used by the Department of Justice to trigger scrutiny or investigation of mergers should be conducted. We believe the study should focus on current threshold levels, why they are used, and most importantly, whether they're applicable to a market for highly perishable products such as livestock. We estimate such a study could be completed for $150,000.

In summary, MPBC realizes guaranteeing U.S. agricultural producers have a fair, transparent, and competitive market for their products is a huge and continuing challenge. MPBC is ready and willing to work with you and the subcommittee on agriculture concentration issues.

Before closing, Mr. Chairman, I want to also point out that USDA is still not to date fully carried out its full legislative mandate under Mandatory Livestock Reporting Act of 1999.

To its credit, USDA is making progress on a number of the mandated programs including the mandatory price reporting system,

the monthly hogs, and PGGs report and improved retail meat price data.

But some mandated programs like the required reporting of separate counts that barrow, gilt slaughter and yard alleys have even to be designed. If this was due to funding, we would urge this committee to rectify the situation at once.

PREPARED STATEMENT

Mr. Chairman, cooperation driven by information and knowledge rather than concentration is the key to finding reasonable long term solutions to the complex issue of ag concentration.

That concludes my comments. Thank you for the opportunity to share National Pork Producers' views on this important issue.

[The statement follows:]

PREPARED STATEMENT OF JON CASPERS

Mr. Chairman and Members of the Subcommittee: My name is Jon Caspers. I am a pork producer from Swaledale, Iowa and serve as the Vice-President of the National Pork Producers Council (NPPC). Today, I am representing America's pork producers and am pleased to discuss with you what we believe is a growing, critical need for Federal government investment and action regarding agriculture concentration.

Agricultural concentration is a difficult and emotionally charged issue. It has become more-so as congressional committee after congressional committee has held hearing upon hearing and yet done little tangible work to even understand the critical issues. Many pork producers are concerned about their ability to continue to compete and maintain market access in a hog market that is experiencing increasing levels of concentration. We need your help in understanding the relevant issues in order to take appropriate actions to assure an efficient marketplace that accurately rewards producers while providing an abundant supply of affordable, safe, nutritious pork.

PORK INDUSTRY CONCENTRATION

Allow me to update you and Subcommittee members on the current status of concentration and vertical coordination in the pork industry.

Concentration in the pork packing sector as measured by the 4-firm concentration ratio (CR–4) grew from 32.2 percent in 1985 to 56.3 percent in 1998. GIPSA's 2000 Annual Report shows a CR4 of 56 in 1999. The market shares of Smithfield, IBP, Swift and Excel are currently included in this measure of total market share. The eight-firm concentration ratio now stands in excess of 75 percent. While not a guarantee of non-competitive conduct that increases consumer prices and/or reduces producer prices, these levels and their trends increase the possibility of such conduct and provide ample incentive for ongoing research and heightened vigilance.

The CR–4 for the hog production segment has grown from negligible levels in the early 1980s to about 18 percent following the 1999 acquisition of Carroll's Foods and Murphy Family Farms by Smithfield Foods and the 2000 purchase of Lundy's by Premium Standard Farms. The market shares of Smithfield, Premium Standard Farms, Seaboard and Prestage comprise this figure.

Vertical integration of packers owning hogs has grown from an estimated 6.4 percent in 1994 to roughly 24 percent today. Smithfield, Premium Standard Farms, Seaboard, Excel, and Farmland are the companies contributing the most to this total. The recent efforts of Tyson Foods and Smithfield Foods to buy IBP, Inc. brought this topic back to the forefront. I also submit a research paper commissioned by NPPC and authored Dr. Clem Ward of Oklahoma State University, Dr. Steve Meyer of NPPC and Dr. Azzadine Azzam of the University of Nebraska as part of the official record of this hearing. I believe it provides valuable insight into the relevant economic issues that should be considered in cases of mergers, especially those that involve vertical integration as well.

In addition to increasing vertical integration (which NPPC defines as actual ownership of hog production by a packer or of packing by a hog producer), vertical coordination through marketing contracts is increasing rapidly. As recently as 1994, 71 percent of the hogs were sold on the cash market transactions and only 20 percent were sold using a price formula. In January 2001, 82.7 percent were purchased

through some type of contractual marketing agreement and 17.3 percent were cash market purchases. This trend has reduced the size of the negotiated hog market substantially and caused many concerns about the efficiency and accuracy of the today's price discovery process. These concerns become even more acute when one considers that the price of the 17.3 percent of hogs sold through cash market transactions directly sets the price for an additional 54 percent of all hogs that are sold on formula-priced contracts.

WHAT SHOULD CONGRESS DO

Firms are getting larger and controlling larger market shares at every level of the pork industry, including production, packing, processing and retailing. There is no doubt that this increased concentration increases the possibility for non-competitive behavior. To that end, the Federal government must be diligent and aggressive in enforcing the Sherman Act, Federal Trade Commission Act, Clayton Act and Packers and Stockyards Act. We urge the Congress and the Administration to clearly communicate their resolve for such aggressive enforcement and, wherever appropriate, to act upon that resolve.

Attacking perceived agriculture concentration problems with a regulatory or judicial axe may not, however, be as beneficial as sharpening that axe with more knowledge about today's firms and systems and how they work. In fiscal 1992, Congress appropriated $500,000 for USDA to conduct a study of concentration in the red meat packing industry. The vast majority of these funds were spent investigating the fed cattle and fed beef segments which were (and still are) among the most highly concentrated in agriculture.

Since that time, though, the pork industry has changed more rapidly and more dramatically than virtually any other agricultural sector. NPPC has repeatedly asked Congress to pay the same kind of attention to the knowledge and understanding level of pork industry that it paid to the beef industry in 1992. As forcefully as respect for the members of this committee will allow, I renew that request today. Specifically, NPPC implores this committee to approve appropriations for the following research:

—*Hog Market Structure & Competitiveness Study.*—The Department of Agriculture should fund studies on hog market structure and competitiveness issues within the pork industry, outlining present realities, future scenarios and the implications for producers' economic wellbeing and our nation's food supply. These studies would be similar to those done in the early 1990s for beef. We estimate that they would cost $750,000.

—*Study of Justifiable Price Differentials.*—To establish a yardstick against which claims of price discrimination could be compared, the Department of Agriculture should fund a study the factors that comprise economically justifiable price differentials, including factors such as volume, time of delivery, carcass specifications, etc. Such research may involve detailed work on packing plant and packing firm economics, a portion of which NPPC has already initiated and would be willing to share with USDA researchers as part of a comprehensive research effort. We estimate that this project could be completed for $400,000.

—*Study of DOJ Concentration Threshold Levels.*—A study of the threshold levels of standard concentration measures (Herfendahl-Hirshman Index, Concentration Ratios, etc.) used by the Department of Justice to trigger scrutiny or investigation of mergers should be conducted. We believe the study should focus on the current thresholds, why they are used and, most importantly, whether they are applicable to a market for a highly perishable product such as livestock. We estimate that such a study could be completed for $150,000.

In addition to funding these projects, Congress should stipulate that they be carried out in a timely fashion. The study of meat industry concentration funded in fiscal 1992 was published in February 1996 largely due to delays in program implementation and to lengthy reviews within USDA that many observers felt were unnecessary. These delays invited criticism of the work even before it was published and, we believe, unfairly reduced its credibility. It was a piece of outstanding economic research that was discredited because of an appearance of timidity and uncertainty. When you fund these pork industry projects, please do everything in your power to see that they do not meet the same fate.

SUMMARY

NPPC realizes that guaranteeing U.S. agricultural producers a fair, transparent and competitive market for their products is a huge and continuing challenge. NPPC is ready and willing to work with you and the Subcommittee on agriculture concentration issues.

Before closing, Mr. Chairman, I want to also point out that USDA has still not, to date, fully carried out its full legislative mandate under the Mandatory Livestock Reporting Act of 1999. To its credit, USDA is making progress on a number of the mandated programs, including the mandatory price reporting system, monthly hogs and pigs reports and improved retail meat price data. But some mandated programs, like the required reporting of separate counts of barrow slaughter and gilt slaughter, have, to our knowledge, yet to even be designed. If this is due to funding, we urge this committee to rectify the situation at once.

Mr. Chairman, cooperation driven by information and knowledge, rather than confrontation, is the key to finding reasonable long-term solutions to the complex issue of agriculture concentration. Such cooperation can help the industry avoid the negative "unintended consequences" of legislative and regulatory actions that, in the long term, could harm producers in particular and the agricultural industry in general.

That concludes my comments. Thank you for the opportunity to share pork producers' views on this important issue.

Senator COCHRAN. Thank you for your testimony and your solutions.

We'll now hear from Mr. David Reiff representing the National Grain and Feed Association.

STATEMENT OF DAVID S. REIFF, PRESIDENT, REIFF GRAIN AND FEED, ON BEHALF OF THE NATIONAL GRAIN AND FEED ASSOCIATION

Mr. REIFF. Thank you, Chairman Cochran, Ranking Member Kohl, and distinguished members. I am Dave Reiff, president of Reiff Grain and Feed, Fairfield, Iowa. I appreciate this opportunity to speak today on this important issue.

First, a little bit about my company. Reiff Grain & Feed is a country elevator firm in southeast Iowa, about 100 miles from Des Moines. We offered feed milling, seeds, and agronomy services to a few hundred family farms in our area.

We originate grain from these producers and offer it back out to our livestock feeders as well as several exporters on the mid Mississippi and several processors in the area.

Reiff Grain & Feed is a member of the National Grain and Feed Association on whose board of directors I serve and on whose behalf I'm testifying.

Agribusiness consolidation today is one of the hottest topics in rural America. There's no doubt that grain businesses are consolidated at the most integrated and capital intensive level of the industry: Food processing and manufacturing. This reflects a trend that is occurring in every part of the economy.

As my written testimony explains in greater detail, however, more important distinctions must be made between not only the manufacturing first purchaser levels of the field but also between the various user segments in the grain marketplace.

In many cases there are dozens of separate potential first purchasers for producers to market their grain to. Country elevators, export elevators, warehouses, river terminals, on farm buying are all customers of farmers.

In wheat country, it is not uncommon for elevators to be no more than 20 miles apart. In corn areas, 10 miles is typical. In my part of Iowa there are six elevators within a 30-mile radius.

Further, cash and futures prices for thousands of markets are posted around the clock on several different information networks with truck, rail, river modes of transportation directly competing in many areas, producers are able to move their crops to the most at-

tractive market at reasonable rates. Competition, transparency, and accessibility make for a highly competitive marketplace.

In addition, competition between various segments of the industry is intense. Domestic and export users of grain must vie for producer's business. There is fierce competition between different domestic users, country elevators, feed mills, feeders, processors, and industrial users.

I would like to mention a matter that is related to the concentration issue. Much attention has been focused on the practice of contracting between producers and agribusiness firms. Cash grain contracting is the most important price risk management tool used by grain farmers today. I urge Congress to be very cautious in legislating how commerce is going to be conducted because there can be some negative unintended consequences.

For example, our local hog producers have an opportunity to enter into a contract that will allow them to benefit in part of the retail margin if the packer is successful with a branded approach in the marketplace.

But now that producer benefit would be in danger of possibly not passing scrutiny by the State attorney general's office if produced Iowa legislation passes.

The competitive advantages contained in this contract may be viewed as secret clauses, thus disallowing the contract.

However, if the competitive advantages are made pubic, they may no longer have value to the producer in the marketplace. Our farm producers badly need new opportunities to stay viable.

Another instance, the local feed lot operator is contracting privately with a cattle finishing corporation to provide yardage services. This seems to be very beneficial to both parties. I hope this new partnership isn't stopped by a requirement that terms their agreement be made public under the new contracting proposal.

Thus while contracting legislation may be well intentioned, there's a high probability of doing more harm than good. I would like to submit to the record a white paper prepared by the National Grain and Feed Association that goes into more detail on this issue.

PREPARED STATEMENT

In conclusion, I would like to emphasize to the subcommittee that while consolidation is occurring at the top level of grain handling industry, producers have access to a competitive, available, and transparent market. Thank you again. I will be pleased to try to respond to questions.

[The statement follows:]

PREPARED STATEMENT OF DAVID S. REIFF

INTRODUCTION

Chairman Cochran, Ranking Member Kohl, and Members of the Subcommittee, my name is Dave Reiff, and I am president of Reiff Grain and Feed, Inc., of Fairfield, Iowa. Thank you for this opportunity to testify on the important subject of consolidation in the agriculture economy, as it relates to the grain sector.

Reiff Grain & Feed, Inc. is a 25 year-old country elevator in Iowa, about 100 miles southeast of Des Moines. We offer feed milling, seeds, and agronomy services to a few hundred family farms in our area. We originate grain from these producers and

offer it out to our livestock feeders as well as several exporters on the mid-Mississippi and several processors in the area.

I appear today on behalf of the National Grain and Feed Association, of which my firm is a member. The NGFA consists of about 1,000 grain, feed, processing and grain-related companies that operate 5,000 facilities that store, handle, merchandise, mill, process and export more than two-thirds of all U.S. grains and oilseeds. About 70 percent of NGFA member firms are small businesses-country elevators and feed mills. Also affiliated with the NGFA are 36 state and regional grain and feed associations.

My testimony today will demonstrate that while many factors are driving integration within the grain sector, competition among the various segments within the industry remains strong; that the grain market is highly transparent; and that substantial competition exists at the first purchaser level for grain.

WHY IS CONSOLIDATION OCCURRING

Every industry in the U.S. and around the globe is consolidating, particularly those industries that are mature and driven by competitive pressures to reduce cost. The U.S. has 3 automobile manufacturers, two major farm implement manufacturers, 4–5 major airlines, etc. Consolidation (both horizontal and vertical) in grain, feed and food processing industries is being driven not only by cost competition, but also by other factors including:

A shrinking farmer customer base.—While the number of total farms in the U.S. seems to have leveled off, the number of commercial farms (those with $100,000 or more in gross sales) continues to decline. With a shrinking customer base, fewer firms are necessary.

Incentives to provide enhanced services to producers.—Firms are offering more services to producers in order to build affinity and retain them as customers. Some examples include tailored risk management plans, farm input consulting, application services, and record keeping. This trend requires greater expertise and manpower on the part of the grain handler.

Consolidation in rail transportation.—There are now only 7 major grain-hauling railroads in the U.S. Rail accounts for 25 percent of commercial grain shipments. Consolidation in the rail industry has resulted in many "captive shippers," or facilities that are served by only one railroad and have limited access to alternative and price-competitive modes of transport. This situation has resulted in many grain firms having to operate facilities on separate rail lines in order to ensure service in case of disruption or uneconomic pricing on one line. In addition, the move toward lower rail rates for larger shipment sizes has been accelerating. This trend saves producers money in shipping to destination markets, but requires grain facilities to increase their capacity to load.

Low rates of return among grain buyers/handlers.—This trend has been documented in several government studies. Low rates of return push individuals to compete or leave the industry and sell out to larger companies.

Compliance with government regulations.—The increasing number and complexity of government regulations tend to drive investment and operational costs higher. Larger companies are required simply to support the resources needed for regulatory compliance.

In addition, vertical integration and increased coordination in the marketing/production chain is being driven by the need to provide both more uniformity and more customer choice at the retail customer level. In today's food marketplace, to meet the uniformity parameters necessary for retail product consistency requires considerably more management control over production, delivery and quality specifications of raw and semi-processed products at each stage of the food chain. Some firms are choosing to obtain this increased management control through ownership—full vertical integration of a company and its products going from raw materials through the final food product.

However, there are other firms that are taking different approaches. Through joint ventures, sharing of resources to jointly coordinate portions of the production-delivery stream for food, and through the use of contracts that require tight quality specifications and just-in-time delivery provisions, companies do have the option to achieve retail product uniformity without full vertical integration.

COMPETITION WITHIN THE GRAIN SECTOR IS STRONG

The heaviest concentration in some segments of the grain and processing sector tend to occur at levels that require extensive capital investments—oilseed crushing, flour milling, wet corn milling, and dry corn milling. However, the fact that fewer than 10 firms in each of these sectors own or operate a high proportion of processing

capacity does not mean that markets into which farmers sell product are lacking in competition. The chart below reflects the percentage market share of each major commodity moving into various markets.

As an example, wet corn milling, which produces starch, corn sweeteners, corn oil and livestock feed, accounts for about 15 percent of total corn markets. There are fewer than 10 firms in the entire U.S. corn wet milling industry, but these wet corn mills have to compete against a large number of feed manufacturers and livestock producers, dry corn millers, and exporters in bidding for corn. Considering that grain markets are truly global in competition, the fact that the U.S. produces less than 25 percent of all major grains indicates that foreign competition and global markets have considerable influence on the pricing of grain. This global influence tends to be reflected in futures market prices in Chicago, Kansas City and Minneapolis, which in turn affect cash prices offered on a given day.

U.S. MAJOR GRAINS AND OILSEEDS

[Percentage Market Share]

	Domestic		Export	Total	U.S. Prod. As Percent of World Market
	Animal Feed	Food/Industrial			
Corn	59	20	21	100	[1] 31
Wheat	12	40	48	100	11
Soybeans [2]	[3] 62	38	100	[1] 29	

[1] "Corn" percentage is actually a percentage of U.S. production of all coarse grains that compete mostly for animal feed markets (other coarse grains include oats, barley, sorghum, and millet). "Soybean" percentage is actually U.S. production of all oilseeds compared to the world (competing oilseeds include sunflower, rapeseed, cottonseed, and palm).

[2] Soybeans crushed (processed) subsequently go into food products (both oil and protein), animal feed (protein meal), and a wide range of industrial use markets.

[3] Domestic crush

THE GRAIN MARKET IS HIGHLY TRANSPARENT

The U.S. has three public futures exchanges: the Chicago Board of Trade, Kansas City Board of Trade, and the Minneapolis Grain Exchange. Thousands of buyers and sellers within the U.S. and throughout the world openly participate and compete in these markets daily, with current price information communicated on a global basis. For many years this public market pricing information has been available through daily newspapers and radio/television news services. Now in the electronic age, public futures exchange prices are available through very affordable computer link services through the internet or via firms such as Data Transmission Network (DTN), Future Source Bridge, Commodity Quote Graphics, and Reuters. Some of these services, in addition to providing futures market price information, also offer cash grain market prices and bids. For example, DTN releases daily cash market prices from more than 2,000 locations in the U.S., updated around the clock. This information reaches more than 100,000 customers across the country. Similar data are available through other electronic, voice and print media.

This very public and highly competitive method of price discovery gives every farmer in the U.S. a strong indication of the value of the commodity that he/she produces or holds in storage on a daily basis.

COMPETITION IS STRONG AT THE FIRST PURCHASER LEVEL

There are many options for producers when it comes to potential customers for their product. The chart below contains a rough estimate of the customers and facilities available to producers in key states:

	Co-op/farmer-owned firms	Co-op/farmer-owned facilities	Private firms	Private facilities
Illinois	162	473	198	578
Indiana	20	93	111	260
Iowa	104	209	134	326
Minnesota	124	135	280	320
Kansas	107	122	133	288
Nebraska	56	242	74	156
North Dakota	150	300	40	140

	Co-op/farmer-owned firms	Co-op/farmer-owned facilities	Private firms	Private facilities
Oklahoma	84	41	182	93
Pacific/Northwest	208	112	715	385

In corn growing states, it is common to have competing elevators located within 10 miles of each other; in wheat states, 20–25 miles between elevators is typical. In some areas, there are also grain buyers who travel to farms by truck and buy from the producer on-site.

It must be recognized that while grain and oilseed processors and exporters often purchase grain directly from farmers, the companies tend to buy the majority of their raw material from independent local businesses operating elevators owned by private entities or farmer cooperatives. These "first buyers" that purchase grain directly from farmers participate in an intensely competitive, nearly atomistic industry.

In addition, farmers' marketing alternatives are expanding. Since grain can be trucked at affordable rates over substantial distances—by hauling companies or producers themselves—producers can access the highest-return markets, including elevators, river terminals, or processors. This increases the competition among grain merchants for customers, to the benefit of the producer. With regards to grain storage, producers are as much competitors in the market as are grain merchants. Commercial storage in the U.S. is estimated at 8 billion bushels, while on-farm storage is more than 11 billion. Farmers must manage the risk of quality deterioration, and the costs of placing the grain in storage plus retrieving it, but the overall effect of on-farm storage is a competitive alternative for the producer to either commercial storage or spot sales.

CONCLUSION

The grain industry, like the rest of the economy, is consolidating. This is occurring for many reasons, not the least of which is to provide better and more cost-effective service to producer-customers. This does not mean, however, that competition is lacking. To the contrary, it is evident that robust competition exists at the first buyer level and among the sectors of the industry; and that grain markets are highly transparent. These factors work together to ensure competitive markets remain the norm for grain farmers in the U.S.

This concludes my testimony. Thank you.

Senator COCHRAN. Thanks, Mr. Reiff. And the study you referred to will be printed in the record. We thank you for submitting that.

Mr. Fred Stokes, President for the Organization for Competitive Markets. Welcome.

STATEMENT OF THOMAS F. STOKES, PRESIDENT, ORGANIZATION FOR COMPETITIVE MARKETS

Mr. STOKES. Thank you, sir. Senator Cochran, Senator Dorgan, I appreciate the opportunity to appear before this hearing on a subject that we believe is at the center of the current farm crisis. I'll make my remarks brief. And I ask that my more detailed written testimony be included in the record.

The organization for competitive markets is a multi-disciplinary non-profit group of farmers, ranchers, academics, attorneys, business people, and State legislators working for a fair, open, and competitive agricultural marketplace. We see market concentration as a major impediment to bringing about such marketplace.

The organization for competitive markets is among some 65 organizations that have advocated a separate title in the new farm bill dealing with competition issues. Included in my written testimony is our statement on this subject, and we hope that it will be considered as this new bill is written.

Last year the merger of Cargill and Continental Grain was finalized. Now Archer Daniels Midland is buying the grain-handling fa-

cilities of Farmland, increasing their already dominant position in grain market.

Essentially Cargill and ADM will come together and constitute the market for grain. The proposed merger of Tyson with IBP failed, though for reasons that are not completely clear. IBP stock has since plummeted.

It looks like Smithfield might make another attempt to buy the world's largest beef packer and the second largest pork packer. Given recent history, it would say that such a merger would be approved.

The concentrated and non-competitive marketplace systematically and increasingly short changes farmers and ranchers. Major packers made four times their normal earnings when we had 8 cent hogs.

In a State legislative hearing when asked by a State senator if they couldn't pay producers more in light of their windfall profits, a representative of one of the major packers said he didn't recall getting a Christmas present from any pork producer.

In addition to concentration, there is the matter of vertical integration. Dr. Neil Harl at Iowa State has dubbed concentration and vertical integration the deadly combination. They bring about contract farming. Company tractor drivers and hog house janitors replacing family farmers. Some call this chickenization.

Vertical integration through contracts give processors and packers captive supplies. Captive supplies, in return, result in fewer bitters and more passive bitters. Spot market prices are lower, volume is also lower, and the resulting thin market more subject to manipulation.

Consolidation in another area also robs farmers of their rightful share of the consumer dollar. In 1964, President Johnson established the National Food Marketing Commission. The report from the commission concluded, among other things, that retail food chains were rapidly emerging as the dominant player in the food marketing system.

And in this study entitled Consolidation and Food Retailing and Dairy, published January the 8th of this year, Dr. Bill Heffernan pointed to the very rapid consolidation of the retail food industry over the past three years, and he stated retailers are now in a position to dictate terms to food manufacturers who then force change back through the system at the farm level.

Dr. Keith Collins, who testified in the earlier panel, is on record as seeing retail margins as a problem. To get some sense of how retail margins have escalated and have affected farm gate prices, I have provided a chart which is very similar to Senator Dorgan's chart which shows the relationship between retail prices and the farmers—and the price farmers receive.

And I might add contrary to some testimony that's already been given here, we would contend that this gap is not because of food that is of higher quality or has been added. A whole light of—beef would be an example. The retailer got a lower margin for beef back in the days of hanging carcasses than it does today when it gets it in box form which greatly decreases his cost of processing.

So it's not necessarily true that these—that this gap is because of these margins or because of the extra things the retailer does.

In September of last year, ERS calculated that the retail margin from the single steer was $722. Obviously this is out of line. A significant portion of this should have gone to the producer but went to the retailer because of his sell it or smell it market power.

I realize the committee is not tasked with regulating retail margins. You can, however, help foster a new marketing system which provides a new route from the farm gate to food consumers and gives producers a fairer share of the end value.

Programs such as the Value-Added Grant Program authored by Senator Grassley. The new generation cooperatives offer promise for a system that would reverse the drastic decline in the farmer's share of the food dollar.

Global markets, mad cow disease, and the seemingly more frequent incidence of food-borne illness have raised new concerns about food. Consumers now want to know more about where their food comes from and how it was handled.

Consumers have more confidence in food that was produced and handled under the more stringent requirement in this country. It's time we had country-of-origin labeling.

Free trade is not turning out to be the panacea it was represented to be. It also raises the issue of food security. Going to the low cost provider in the global marketplace for our food makes about as much sense as having our more advanced military weaponry made in China. We need markets that are established and maintained in consonance with the original intent of our antitrust laws.

Enforcement agencies should be headed with people who desire to enforce these laws, and Congress should give them the necessary resources to do their job. We need transparent markets.

PREPARED STATEMENT

Open, transparent, and competitive markets for agriculture are our best bet for just recompense for those that tend the flocks and till the soil. And for a safe, dependable, and affordable food supply for our people. And I'll be happy to respond to any questions.

[The statement follows:]

PREPARED STATEMENT OF FRED STOKES

INTRODUCTION

Thank you for this opportunity to present testimony on agricultural concentration issues. The Organization for Competitive Markets (OCM) is a multidisciplinary nonprofit group of farmers, ranchers, academics, attorneys, businesspersons and state legislators working for a fair, open and competitive agricultural marketplace. OCM is the only nonprofit organization in the country with a primary focus on antitrust and trade practices policy in agriculture. This testimony is submitted to enhance informed discussion on the propriety, and contents, of a Competition Title in the next Farm Bill. Sixty-five organizations have signed a letter in favor of including such a Competition Title. (See Exhibit B, Letter to Sen. Lugar, May 1, 2001).

Family farmers ultimately derive their income from the agricultural marketplace. These independent producers have always been in a position of weakness in selling their product to large processors and in buying their inputs from large suppliers. Though there has been a tremendous focus on openness and competition in the export markets, the domestic marketplace has become closed and noncompetitive. Today the position of the family farmer has become even weaker as consolidation in agribusiness and food retail has reached all time highs. Farmers have fewer buyers and suppliers than ever before. The result is an increasing loss of family farms and the smallest farm share of the consumer dollar in history.

The Agricultural and Food subeconomy can be divided into four sectors: 1) agricultural input suppliers; 2) farmers, ranchers and growers; 3) processors and packers; and 4) food retailers. All but the farm sector have experienced unprecedented consolidation in recent years, surrounding farmers with 800 pound gorillas that are able to squeeze farm income to zero. The result is that no matter the level of income, even with the doubling of Federal support, farmers' income languishes. Congress must comprehensively address this problem by confronting the problems inherent in consolidation and vertical integration.

One hundred years ago, this nation reacted appropriately to citizen concerns about large, powerful companies by establishing rules constraining such businesses when they achieved a level of market power that harmed, or risked harming, the public interest, trade and commerce. The United State Congress enacted the first competition laws in the world to ensure that commerce remain free and fair. These competition laws include the Sherman Act, Clayton Act, Federal Trade Commission Act and Packers & Stockyards Act. Since that time, many countries in the world have followed this U.S. example to constrain undue market power in their domestic economies.

DANGERS POSED BY A CONSOLIDATED AND VERTICALLY INTEGRATED FOOD AND AGRIBUSINESS SECTOR

Unfortunately, competition policy has been severely weakened in this country, especially in agriculture, due to Federal caselaw, underfunded enforcement, and unfounded reliance on efficiency claims. These weakening factors have resulted in a significant degradation of the domestic agricultural market infrastructure. For instance, the cattle, hog and poultry sectors all have structures ripe for unfair methods of competition by the packer or processor. In cattle, the top four slaughter firms control over eighty percent of the market, with IBP, Inc. controlling thirty two percent of the steer and heifer market. The top four hog packers control about fifty-six percent of the market, including Smithfield with over eighteen percent. The poultry industry is similar to hogs, with Tyson controlling over a quarter of the market. This trend toward consolidation continues. Just recently IBP was the subject of a bidding war between Smithfield and Tyson. ADM announced that it plans to take control of Farmland's grain assets throughout the U.S. Purina announced that it is in discussions with a suitor to sell its assets.

The dangers posed by horizontal concentration are exacerbated by the spiraling vertical integration in these industries. Vertical integration, where one firm controls numerous sectors in the production cycle, has long been utilized in poultry. In that industry, poultry integrators installed a system in which the processor owns the chickens; and the grower owns the land, buildings, equipment, chicken litter and the dead chickens. The same dynamic has overtaken the hog industry. Only about seventeen percent of all hogs were marketed on the open or spot market in 2000. The rest of the hogs are either owned by packers or contracted in advance so the packer avoids the open market. With the emergence of genetically modified crops and the seed company's monopoly control of life forms, these companies increasingly utilize exclusive vertical relationships to maintain control of their product.

These trends have led to what Professor Harl calls "the deadly combination of concentration and vertical integration." The combination of the two leaves the producer in an unenviable position: suddenly he has very few, possibly one, processor with whom to deal in his region, and no open market to send his product. Nevertheless, financers and other agricultural advisors have short-sightedly urged farmers to lock themselves into contracts, thinking that abandoning the open market would allow the farmer, and the bank, to circumvent risk. The price risk of the open market might have been avoided; but the increased risk of unfair and anticompetitive practices was ushered in with the proliferation of contracts.

The result of contracts on the aggregate market is that processors and packers now have captive markets. Captive supplies result in not only fewer bidders, but the remaining bidders are much more passive because they have captured supply through non-price means: forward contracts, production contracts, marketing agreements and packer and processor ownership. This gives the processor more control over inventory while transforming them into passive bidders that can procure the balance of their supply through conservative bidding. Spot market transactions are priced lower, are lower in volume, and the thin market increases the risk of manipulation. (For a thorough discussion of the dangers of captive supply and the USDA authority to address these dangers, see Exhibit A, Written Testimony of Organization for Competitive Markets Before the USDA's Public Forum on Captive Supplies in the Livestock Sector, Denver, Colorado September 21, 2000, also at http://www.competitivemarkets.com/library/testimony/gipsa/GIPSA.OCM.web.092100.htm.)

Yet another sector that funnels the food dollar away from farmers is the food retail sector. The margin that retailers have retained of the consumer dollar has soared, while the farmers' share has plunged. Consolidation in food retail has also harmed consumers. The top five food retailers in the United States now account for 42 percent of all sales. This number has skyrocketed from 24 percent in 1997. Regionally, consolidation and its effects are even more stark. For instance, Dr. Ron Cotteril, of the University of Connecticut Food Marketing Policy Center, recently released a case study on consumer milk prices in the Northeast that showed three supermarkets accounted for 85 percent of all milk sales. At the same time that the retail sector was consolidating, consumer milk prices steadily increased. The study concluded that a $50 million increase in the milk bill paid by consumers is due exclusively to the market power of private companies, i.e. supermarket retailers and dairy processors.

We urge Congress to strengthen competition and trade practices policy by enacting legislation that protects family farmers from anticompetitive and unfair practices. Over 65 groups including OCM have joined together recently to urge Congress to create a Competition Policy title in the farm bill. (See Exhibit B, Letter to Sen. Richard Lugar, May 1, 2001). Congress must address the disparities in market power at the same time that it considers provisions to improve farm income. Otherwise, input suppliers, processors and retailers will continue to reap farmers' share of the food dollar.

RECOMMENDATIONS FOR IMPROVED POLICY AND ENFORCEMENT

OCM believes that Congress needs to take a comprehensive approach in addressing the complicated problems associated with concentration and vertical integration. For purposes of analytical discussion, we have divided our recommendations into four areas: Antitrust policy and enforcement; competition and trade practices policy and enforcement in the livestock sector; fairness in contracting; and creating new competition.

Antitrust Policy and Enforcement in Agriculture

General antitrust laws, such as the Sherman, Clayton and FTC Acts were originally intended to hinder huge firms from exercising undue market power. The Federal judiciary and past administrations have gutted the enforcement of these laws. The Department of Justice and the FTC woefully lack the resources to address the explosion of mergers and increased consolidation. The policies and court interpretations of these laws intended to protect consumers, small businesses and farmers have degraded to the point where Congressional clarification is required. Enforcement officials and judges have been too quick to blindly accept efficiency arguments, without proof, while ignoring the plight of small businesses and independent suppliers such as farmers.

To breath life back into antitrust policy, Congress should:

—Clarify that the antitrust laws focus on supplier harm in addition to consumer harm;

—Enact new legislation to prohibit mergers or acquisitions that allow a firm to gain more than a fifteen percent market share nationally in any agricultural business, including the retail supermarket trade. This allows firms to reach peak efficiencies of scale without achieving the dominance which has anti-competitive results;

—Create and fund an Office of Agricultural Competition in the Department of Justice to increase the resources and talent available at DOJ for agriculture;

—Amend the Clayton Antitrust Act to make it clear that a person who suffers indirect or pass-through harm can recover damages resulting from anti-competitive conduct (repeal the Illinois Brick decision);

—Enact legislation easing the ability of farmers to achieve class status in litigation involving anticompetitive practices by agricultural businesses, including the retail supermarket trade; and

—Significantly increase funding for enforcement of antitrust laws generally.

COMPETITION AND TRADE PRACTICE POLICY AND ENFORCEMENT IN THE LIVESTOCK SECTOR

Congress has long recognized the special nature of the livestock industry and the increased likelihood that packers and processors will treat farmers and ranchers unfairly. In 1921 Congress passed the Packers and Stockyards Act to address the problems inherent in a consolidated packing industry that had vertical relationships with the marketing channels of the day, the stockyards and rail lines. Although OCM and others have long argued that sufficient authority exists within the far-

reaching Act to affect real change in the livestock industry, the USDA has not acted. Farmers and ranchers can wait no longer. Congress must step in to prohibit deleterious practices associated with the consolidated and vertically integrated sector. It has been eighty years since a Congress substantively affected the P&S Act. Congress must act again.

We urge Congress to:

—Consider transferring jurisdiction over competition issues in the livestock sector from the United States Department of Agriculture to a newly created Office of Agricultural Competition in the Department of Justice;
—Prohibit red meat processors from owning livestock or livestock production operations;
—Enact a two-year suspension on mergers and acquisitions between firms in the red meat and poultry processing sectors;
—Create an transparent, fully functioning market in livestock contracting through requiring all contracts to be offered for bidding in an open, public manner and necessitating that a fixed base price be negotiated at the time of the agreement (as opposed to formulating the price from another market);
—Declare discrimination in non-price procurement terms by processors as to producers as anticompetitive or discriminatory practices unless such benefits are offered to all in an open, public manner. Such non-price benefits include, but are not limited to, delivery terms, processor financing, and processor leasing/ownership of facilities or land;
—Provide poultry growers with full protection under the P&S Act; and
—Increase transparency and full information in the marketplace by eliminating the 3/60 rule from the administration of mandatory price reporting by the USDA Market News Service.

FAIRNESS IN CONTRACTING

Contracting provides packers and processors relational market power. A number of ways exist for a firm to exert this "lock-in" power: (1) packers exploit farmer's sunk costs reasonably incurred in connection with carrying the packer's contract requirements; (2) the packer imposes additional costs on a disfavored farmer; and (3) the packer refuses to offer the farmer favorable business opportunities available to other farmers. Examples of this type of market power abound in both the poultry and hog contracting sectors. This market power provides the packing and processing firms the ability to pressure farmers and growers in a number of ways. Contracts that require substantial investment for a packer's particular requirements put the farmer at risk of exploitation in the future. These types of contracts are common. In poultry, contracts provide the integrator great discretion in what it may demand as far as capital requirements. In hogs, some packers require that the farmer restock its entire herd with the packer's preferred genetic line, and restrict the farmer from selling offspring of those genetics. Once the farmer has built new buildings for hundreds of thousands of dollars or restocked his entire herd, he is no longer in the position to freely seek other processors with whom to deal. He is set up to serve one particular packer or processor. This "lock-in" effect allows the processor to treat the farmer less favorably in the future and the contracts are written in a way that allows processors to do this. Because the farmer is locked in to the processor's system, he will suffer the injurious conduct because he has no better options.

To the extent that contracting is allowed between agricultural producers and processors, we urge that Congress enact the following provisions:

—Prohibit confidentiality clauses in contracts;
—Require contracts to be in plain language and to disclose material risks;
—Prohibit mandatory arbitration clauses;
—Provide contract producers with a three-day right to review contracts;
—Prohibit unfair practices, including tournament contracts that base pay on a ranking system based on variables outside of the farmers' control;
—Prohibit arbitrary cancellation of contracts that required significant capital investment;
—Provide producers with a first-priority lien for payments due under a contract;
—Protect producers from having contracts terminated capriciously or as a form of retribution; and
—Prohibit processors from retaliating or discriminating against producers who exercise rights including the right to join producer organizations.

CREATING NEW COMPETITION

The establishment of new competitors in the agriculture sector is key to diffusing the power of the dominant firms and providing profitable opportunities for family

farmers. Federal and State governments provide tremendous amounts of money to dominant firms in the form of grants, loans, tax breaks, research and development subsidies. We urge the Congress to redirect much of these funds to spur the development of new start-ups that will provide new opportunities for family farmers to market their products.

—Target most food and agriculture related grant and loan programs to small to mid-sized farms and farmer-owned businesses. This should not be limited to entities structured as cooperatives;

—Focus most research performed within USDA or funded by USDA on small to mid-sized farms and farmer-owned businesses;

—Provide a preference to bids from farmer-owned food entities for government food procurement contracts. Government contracts should also require smaller volumes, as opposed to the large volumes currently included in such contracts, to allow small suppliers to bid. Further, a study should be done to identify barriers to government buying from farm-based or farmer-owned food suppliers in an effort to find and implement solutions to such barriers;

—Increase the level of funding for the USDA Value Added Agriculture grant programs facilitated by Sen. Charles Grassley last year; and

—Foster direct procurement from farmers and farmer-owned entities for the Federal Food Stamp program and Women, Infants and Children program. The electronic funds transfer cards used to transfer moneys and pay food providers in these programs are barriers to farmer participation. These constraints came be overcome.

CONCLUSION

Congress has focused, in recent years, on open and competitive markets at the international level. It should now work harder for open and competitive markets at the farm gate level domestically. It is at the farm gate where producers derive their income from the marketplace. Marketing choices are necessary for a functioning market. Concentration allows private economic power the proven ability to unduly drive farm gate prices down and consumer food prices up. Competition and choice will provide more marketing choices for farmers, fewer barriers to entry for new competition, and prices which more accurately reflect supply and demand. It is time for a Competition Title to be included in the Farm Bill to address these problems in a comprehensive manner.

Senator COCHRAN. Thank you, Mr. Stokes. I appreciate you coming up from Mississippi to be with us today. I've talked with you on the phone several times and in person a couple of times. It's good to have you as part of this panel.

I think we've had a balanced overview from this panel of the different commodity and food group areas that are represented, and we appreciate very much the statements that you have prepared to make a part of this record.

Because we have another panel, and we have some other obligations that are developing on the floor of the Senate, I don't want you to feel like we don't care about you if we don't ask you a bunch of questions. But to hear the other panel and to have them to have an opportunity to speak, our questions are going to be abbreviated.

I just want you to know it won't be an insult to you. I hope you won't consider it as such.

One thing Mr. Stokes mentioned I was going to ask all of the panel about, he referred to cooperatives. And I can remember the time when individual producers decided that that was one of the answers to concentration in the industry groups that were buying farm products and commodities to compete. Farmer-owned cooperatives would be one of the answers.

Isn't it true that that has worked to help provide power in the marketplace to individual farmers? I'll just start with Mr. Caspers and see what your reaction to that is.

Mr. CASPERS. Yes, we're very supportive of farmer-owned cooperatives and some of the new generation cooperatives that are farming. I think there is a lot of interest amongst our members all across the country. MPPC was instrumental approximately two years ago in starting what has developed into pork America.

They continue to develop and have a number of members across the country, and I think on the next panel you have a member of ours that's involved in a pork cooperative venture in Illinois that hopes to go to construction this year.

Senator COCHRAN. Mr. Dopp, what's your view of that?

Mr. DOPP. Well, Senator, I'm not sure I can add much to that other than to comment that one of our large members, in fact Farmland Foods is part of a cooperative, and they have been successful on a number of levels and a number of areas for a number of years.

Senator COCHRAN. Mr. Roenigk?

Mr. ROENIGK. Yes, thank you. As a general statement, agricultural cooperatives are beneficial to agriculture; however, in the broiler industry, for whatever reason, many, many years ago we had several cooperatives. Today we have just one survivor that is a cooperative.

In fact, in the 1980s I think the government helped start at least one if not more cooperatives to see if they worked again, but whatever the dynamics are, they don't seem to work in our industry. But as a general principle, I agree. Cooperatives are a good thing to have.

Senator COCHRAN. Mr. Reiff.

Mr. REIFF. Really not much to add. The Farmland/ADM recent joint venture was mentioned. They obviously found value in linking up, and the cooperative itself was having some difficulty. But I think by and large it probably is viable.

Senator COCHRAN. Mr. Stokes?

Mr. STOKES. Well, I generally agree that they're a good thing. There are some who have run amuck, in my opinion. And I wouldn't necessarily hold Farmland up as an outstanding example of what cooperatives could do.

Senator COCHRAN. One of the industries in our State, a new industry, catfish production, falls away from the processing, the growing of the fish, and the processing, growing grain. Some of these are cooperatives, some are owned by corporate parent companies. Like ConAgra, as a matter of fact, has gotten into that business.

I don't know whether this is less competition. It seems to me that there has been a proliferation of different businesses in that industry. It's a fairly new industry. I wonder if any of you have any comments about that, if you know anything about it, whether you think that's bad or good. It's competing with the chickens probably a little more than they want.

What do you think, Mr. Roenigk?

Mr. ROENIGK. I'm certainly not a catfish industry expert, so I hesitate to speak about the catfish industry. But you're correct that in Mississippi there's a large catfish industry like some of our neighboring States.

The broiler industry is very strong in Mississippi, Arkansas, and many other States. The investment and relationship is probably still evolving in the catfish industry. At some point, a business model probably will emerge where it has some better opportunity to exercise its advantage in the marketplace, whether it is branding or further processing or exporting or whatever.

So, as you say, it's still a new industry. This mix will probably stay for a while until one model beats out another model, not that that will be totally the way the market is, but it's still evolving. I realize that's not a very helpful answer, but that's the best I know.

Senator COCHRAN. I appreciate that, and we appreciate your contribution.

Senator Dorgan.

Senator DORGAN. Mr. Chairman, we have the reconciliation bill and the tax cut beginning to be on the Floor about a half an hour ago, so I'm going to forego questions of the panel.

I think your contributions have provided substantially different perspectives from I guess different viewpoints on these issues, and I think they contribute to our ability to understand how various groups and interests feel about these issues.

So we appreciate the statements you've made. We do have, I think, five or six people on the third panel, and I want to be able to get to that before we have to go to the Floor of the Senate.

Senator COCHRAN. Thank you, Senator. Thank you all for your preparation. We appreciate it very much.

Our third panel of witnesses we would ask to come forward to the witness table. I will introduce them as they are coming forward. Mr. Dudley Butler represents the Mississippi Cattleman's Association.

Robert Carlson is the President of the North Dakota's Farmers Union. Peter Carstensen is Associate Dean for Research and Faculty Development at the University of Wisconsin Madison Law School. Mr. Dan Kelley is an Illinois farmer. Tom Miller is the Attorney General of the State of Iowa, and David Reiss who is President Elect of the Illinois Pork Producers Association.

We have copies of your prepared statements, and they will be made a part of the record in full. I would encourage you to make summary comments from your statement, and then we'll have an opportunity, I hope, to ask you some questions.

Let's start off with our first witness in this third panel, Mr. Dudley Butler.

STATEMENT OF DUDLEY BUTLER, ON BEHALF OF THE MISSISSIPPI CATTLEMEN'S ASSOCIATION

Mr. BUTLER. Mr. Chairman and members of the committee, I appreciate the opportunity you're giving me to testify. As you said, my name is Dudley Butler. I live on my ranch in Yazoo County, Mississippi. I'm also a practicing trial lawyer, arbitrator, mediator, as well as a cattleman.

I serve as cochair of the ADR subcommittee, promotion subcommittee for the Bar Association, and I'm also acting as special assistant to the President of the National Cattleman's Beef Association.

I want to speak to you about the contracts that are used in agriculture now, and most specifically about some of the clauses that are put in those contracts. I believe that arbitration is a valuable alternative to dispute resolution procedure if entered into knowingly and voluntarily.

Under the right circumstances, it can be fair, cost effective, and time saving. Under the wrong circumstances, it is unfair and totally inequitable.

Although I first became involved in the poultry industry while trying to promote arbitration and mediation, I must tell you that at this present time I represent numerous poultry growers in litigation against poultry companies. Part of that litigation involves the attack on mandatory arbitration clauses contained in poultry growing contracts.

Many of these arbitration clauses require poultry growers to waive any right to a jury trial and also contained cost laden provision that make arbitration inaccessible. In other words, the litigation forum is taken away by contract, and the arbitration forum is taken away by economics, thereby leaving the grower with no forum in which to bring his dispute.

These clauses are forced upon growers because they have no other resource than to accept these provisions under duress. They owe large sums of money on their farm and have no other way to repay the loans but to receive chickens from the poultry companies.

Therefore, I feel that the arbitration clauses are being used as a weapon not as a dispute resolution device. This is obviously contrary to the intent of the framers of the Federal Arbitration Act as evidenced by section 2 which states that an arbitration provision in any maritime transaction or transaction involving commerce shall be valid, irrevocable, and enforceable save upon such grounds as exist at law or inequity for the revocation of any contract.

Surely citizens should not be required to waive their constitutional right to a trial by jury while under such duress. As you well know, the constitutional right of trial by jury is as important as freedom of speech, religion, and other rights that were granted by the framers of our Constitution.

I agree with many of my colleagues as well as the learned justices O'Connor and Rehnquist that the Federal Arbitration Act was not meant to apply in State courts. But was meant as a procedural statute to apply in Federal court to certain classifications of businesses as evidenced by the legislative history provided in the dissenting opinion, *Southland Corporation* v. *Keating.*

In *Breman* v. *Zapata Off-Shore Oil Company,* the Supreme Court noted that contract fixing a particular forum for resolution of all disputes was made in an arm's length negotiation by experienced and sophisticated businessmen.

A poultry growing contract is not an arm's length negotiated agreement. Quite to the contrary. As a contract of adhesion presented to the grower on a take-it-or-leave-it basis, poultry growers are not experienced and sophisticated businessmen.

Therefore, my concern that I am presenting to this committee is that the use of mandatory arbitration clauses along with the waiver of any right to a trial by jury is, in fact, counterproductive to the promotion of the arbitration process.

The arbitration process, although meant to be expedient and cost effective, has become extremely time consuming and expensive under the wording of many of the mandatory clauses now used in production contracts.

Do we want a dispute resolution device, or do we want a cost controlling liability reduction device, and therefore an income producing element used in the agricultural industry? Do we want to preclude farmers from having any forum to air their disputes, thereby reducing the cost of operations for large companies and supposedly the cost of goods to consumers?

What price are we willing to pay for cheaper food? Clearly any waiver of a right to a trial by jury must be clear and voluntary. This right is given to criminals, why is it not provided to law abiding hard working farmers?

Mandatory arbitration clauses are also having an extremely detrimental effect to the reduction of litigation in that they are creating a totally new area to be litigated which is in direct conflict with the whole purpose of alternative dispute resolution.

I think there are two simple answers to these complex problems. The first is for the Federal Arbitration Act to be amended to reflect exactly what courts and entities it applies to.

The other is that the act can be amended or additional laws passed to mandate that an individual or entity be allowed to choose his forum, whether it be litigation or arbitration at the time the claim is made.

This is the only time that a knowledgeable and voluntary decision can be made. Just as a yacht is not usable on a five-acre farm pond, a John boat is not usable in an ocean. Decisions concerning proper forums have to be made after the type, complexity, and amount of the claim is known.

We must look to history, for we can't see where we're going unless we know where we've been. This level of concentration in agriculture was experienced in the early 1900s, and arising from those problems was the passage of the Packers and Stockyard Act to protect farmers against corporation concentration. Today we must move to do the same.

One move is the protection of producers against mandatory waiver of trial by jury and mandatory arbitration clauses. I remember early in law school a professor informed me that justice and fairness are not the same thing. He was right. Justice is based on the law, fairness is fueled by wisdom.

The American Bar Association, the American Medical Association, and the American Arbitration Association on the commission on healthcare dispute resolution used such wisdom and found as follows: In disputes involving patients, binding forms of dispute resolution should be used only where the parties agree to do so after a dispute arises. This is the only way to guarantee that the agreement to arbitrate is both knowing and voluntary.

It is necessary to ensure that the parties' constitutional and other legal rights are protected. I wholeheartedly agree with that finding and believe that the only way to assure the successful promotion of arbitration is to ensure that it is voluntary.

I am concluding by citing to you from the book of Isaiah. Isaiah was a great religious and political influence during the reign of King Hezekiah and Juda, and he also served as his chief advisor.

In chapter 10:12, "Woe to those who make unjust laws, to those who issue oppressive decrees to deprive the poor of their rights and withhold justice from the oppressed of my people."

PREPARED STATEMENT

I agree that agriculture is evolving, and I think it's paramount that the laws evolve with it to protect those that are out there producing on the family farm.

I think it is going to develop into almost a national security issue if we do not do something to protect our people that are tilling the soil, raising chickens, raising hogs, raising cattle, and other types of farm.

[The statement follows:]

PREPARED STATEMENT OF DUDLEY BUTLER

Mr. Chairman and members of the committee, I appreciate the opportunity you are giving me to testify. My name is Dudley Butler, I am from Yazoo County, Mississippi where my family and I live on our cattle ranch. I am a practicing trial lawyer, arbitrator and mediator, as well as a cattleman. I serve as co-chairman of the ADR promotions sub-committee for the Mississippi Bar Association and I am currently acting as special assistant to the President of the National Cattlemen's Beef Association.

I grew up in the small town of Batesville, Mississippi living in a household with my Mother and Father, who was a union pipe fitter, and my maternal Grandmother and Grandfather, who was a grocer for Kroger Company. I think that you could say that my Father was a union man and my Grandfather was a company man. My paternal Grandfather was a very poor sharecropper in Humphrey County, Mississippi. I share this with you because I think it has helped me throughout my life to envision both sides of problems that are presented in any litigation or dispute.

I believe that arbitration is a valuable alternative dispute resolution procedure if entered into knowingly and voluntarily. Under the right circumstances it can be fair, cost effective and time saving. Under the wrong circumstances it is unfair and totally inequitable. Although I first became involved with the poultry industry while trying to promote arbitration and mediation, I must tell you that at this time I represent numerous poultry growers in litigation against poultry companies. Part of that litigation involves the attack on the mandatory arbitration clauses contained in poultry growing contracts. Many of these arbitration clauses require poultry growers to waive any right to a jury trial and also contain cost laden provisions that make arbitration inaccessible. In other words, the litigation forum is taken away by contract and the arbitration forum is taken away by economics, thereby leaving the grower with no forum in which to bring his dispute. These clauses are forced upon the growers because they have no other recourse than to accept these provisions under duress. They owe large sums of money on their farm and have no other way to repay the loans but to receive chickens from the poultry companies. Therefore, I feel that the arbitration clauses are being used as a weapon not a dispute resolution device. This is obviously contrary to the intent of the framers of the Federal Arbitration Act as evidenced by Section 2 which states:

"A written provision in any maritime transaction or a contract evidencing a transacting involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such contract, transaction, or refusal shall be valid, irrevocable, and enforceable, save upon such grounds as exists at law or in equity for the revocation of any contract." (emphasis added)

Surely citizens should not be required to waive their constitutional right to a trial by jury while under such duress. As you well know, the constitutional right of trial by jury is as important as is freedom of speech, religion and other inalienable rights that were granted by the framers of our Constitution. I agree with many of my colleagues, as well as the learned Justices O'Connor and Rehnquist, that the Federal

Arbitration Act was not meant to apply in state courts but was meant as a procedural statute to apply in Federal court to certain classifications of businesses as evidenced by the legislative history provided in the dissenting opinion in *Southland Corporation* v. *Keating*, 465 U.S.1(1984) which is as follows:

"Section 2 does not, on it's face, identify which judicial forums are bound by its requirements or what procedures govern its enforcement. The FAA deals with these matters in §§ 3 and 4. Section 3 provides:

'If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration . . . the court . . . shall on application of one of the parties stay the trial of the action until arbitration has been had in accordance with the terms of the agreement . . . .'

Section 4 species that a party aggrieved by another's refusal to arbitrate "may petition any United states district court which, save for such agreement, would have jurisdiction under title 28, in a civil action or in admiralty of the subject matter . . . for an order directing that such arbitration proceed in the manner provided for in such agreement . . . ."

Today the Court takes the facial silence of § 2 as a license to declare that state as well as Federal courts must apply § 2. In addition, though this is not spelled out in the opinion, the Court holds that in enforcing this newly discovered Federal right states courts must follow procedures specified in § 3. The Court's decision is impelled by an understandable desire to encourage the use of arbitration, but it utterly fails to recognized the clear congressional intent underlaying the FAA. Congress intended to require Federal, not State, courts to respect arbitration agreements.

The FAA was enacted in 1925. As demonstrated infra, at 24–29, Congress thought it was exercising its power to dictate either procedure or "general Federal law" in Federal courts. The issue presented here is the result of three subsequent decisions of this Court.

In 1938 this Court decided *Erie R. Co.* v. *Tompkins*, 304 U.S.64. *Erie* denied the Federal Government the power to create substantive law solely by virtue of the Art. III power to control Federal-court jurisdiction. Eighteen years later the Court decided *Bernhardt* v. *Polygraphic Co.*, 350 U.S. 198 (1956). *Bernhardt* held that the duty to arbitrate a contract dispute is outcome-determinative—i. e. "substantive"—and therefore a matter normally governed by state law in Federal diversity cases.

Bernhardt gave rise to concern that the FAA could thereafter constitutionally be applied only in Federal-court cases arising under Federal law, not in diversity cases.

In *Prima Paint Corp.* v *Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404–405 (1967), we addressed that concern, and held that the FAA may constitutionally be applied to proceedings in a Federal diversity court. The FAA covers only contracts involving interstate commerce or maritime affairs, and Congress "plainly has power to legislate" in that area.

Nevertheless, the *Prima Paint* decision "carefully avoided any explicit endorsement of the view that the Arbitration Act embodied substantive policies that were to be applied to all contracts within its scope, whether sued on in state or Federal courts." P. Bator, P. Mishkin, D. Shapiro, & H. Wechsler, Hart and Wechsler's The Federal Courts and the Federal System 731–732(2d ed. 1978). Today's case is the first in which this Court has had occasion to determine whether the FAA applies to state-court proceedings. One statement on the subject did appear in *Moses H. Cone Memorial Hospital* v. *Mercury Construction Corp.*, 460 U.S. 1(1983), but that case involved a Federal, not a State, court proceeding; its dictum concerning the law applicable in state courts was wholly unnecessary to its holding.

The majority opinion decides three issues. First, it holds that § 2 creates Federal substantive rights that must be enforced by the state courts. Second, though the issue is not raised in this case, the Court states ante, at 15–16, n. 9, that § 2 substantive rights may not be the basis for invoking Federal-court jurisdiction under 28 U.S.C. § 1331. Third, the Court reads § 2 to require state courts to enforce § 2 rights using procedures that mimic those specified for Federal courts by FAA §§ 3 and 4. The first of these conclusions is unquestionably wrong as a matter of statutory construction; the second appears to be an attempt to limit the damage done by the first; the third is unnecessary and unwise.

One rarely finds a legislative history as unambiguous as the FAA's. That history establishes conclusively that the 1925 Congress viewed the FAA as a procedural statute, applicable only in Federal courts, derived, Congress believed, largely from the Federal power to control the jurisdiction of the Federal courts.

In 1925 Congress emphatically believed arbitration to be a matter of "procedure." At hearings on the Act congressional Subcommittees were told: "The theory on which you do this is that you have the right to tell the Federal courts how to proceed" The House Report on the FAA stated: "Whether an agreement for arbitration

shall be enforced or not is a question of procedure . . .” On the floor of the House Congressman Graham assured his fellow Members that the FAA “does not involve any new principle of law except to provide a simple method . . . in order to give enforcement . . . It creates no new legislation, grants no new rights, except a remedy to enforce an agreement in commercial contracts and in admiralty contracts.”

A month after the Act was signed into law the American Bar Association Committee that had drafted and pressed for passage of the Federal legislation wrote:

“The statute establishes a procedure in the Federal courts for the enforcement of arbitration agreements . . . A Federal statute providing for the enforcement of arbitration agreements does relate solely to procedure of the Federal courts. . . . [W]hether or not an arbitration agreement is to be enforced is a question of the law of procedure and is determined by the law of the jurisdiction wherein the remedy is sought. That the enforcement of arbitration contracts is within the law of procedure as distinguished from substantive law is well settled by the decisions of our courts.”

Since *Bernhardt,* a right to arbitration has been characterized as “substantive,” and that holding is not challenged here. But Congress in 1925 did not characterize the FAA as this Court did in 1956. Congress believed that the FAA established nothing more than a rule of procedure, a rule therefore applicable only in the Federal courts.”

If characterizing the FAA as procedural was not enough, the draftsman of the Act, the House Report, and the early commentators all flatly stated that the Act was intended to affect only Federal court proceedings. Mr. Cohen, the American Bar Association member who drafted the bill, assured two congressional Subcommittees in joint hearings:

“Nor can it be said that the Congress of the United States, directing its own courts . . ., would infringe upon” the provinces or prerogatives of the States . . . [T]he question of the enforcement relates to the law of remedies and not to substantive law. The rule must be changed for the jurisdiction in which the agreement is sought to be enforced . . . There is no disposition therefore by means of the Federal bludgeon to force an individual State into an unwilling submission to arbitration enforcement.”

The House Report on FAA unambiguously stated: “Before [arbitration] contracts could be enforced in the Federal courts . . . This law is essential. The bill declares that such agreements shall be recognized and enforced by the courts of the United States.”

Yet another indication that Congress did not intend the FAA to govern state-court proceedings is found in the powers Congress relied on in passing the Act. The FAA might have been grounded on Congress’ powers to regulate interstate and maritime affairs, since the Act extends only to contracts in those areas. There are, indeed, references in the legislative history to the corresponding Federal powers. More numerous, however, are the references to Congress’ pre-Erie power to prescribe “general law” applicable in all Federal courts. At the congressional hearings, for example: “Congress rests solely upon its power to prescribe the jurisdiction and duties of the Federal Courts.” And in the House Report:

“The matter is properly the subject of Federal action. Whether an agreement for arbitration shall be enforced or not is a question of procedure to be determined by the law court in which the proceeding is brought and not one of substantive law to be determined by the law of the forum in which the contract is made . . .”

Plainly, a power derived from Congress’ Art. III control over Federal-court jurisdiction would not by any flight of fancy permit Congress to control proceedings in state courts.

The foregoing cannot be dismissed as “ambiguities” in the legislative history. It is accurate to say that the entire history contains only one ambiguity, and that appears in the single sentence of the House Report cited by the Court ante, at 12–13. That ambiguity, however, is definitively resolved elsewhere in the same House Report, see supra, at 27, and throughout the rest of the legislative history.

The structure of the FAA itself runs directly contrary to the reading the Court today gives to § 2. Sections 3 and 4 are the implementing provisions of the Act, and they expressly apply only to Federal courts. Section 4 refers to the “United States district court[s],” and provides that it can be invoked only in a court that has jurisdiction under Title 28 of the United States Code. As originally enacted, § 3 referred, in the same terms as § 4, to “courts [or court] of the United States” There has been a minor amendment in § 4’s phrasing, but no substantive change in either sections’s limitation to Federal courts.

None of this Court's prior decisions has authoritatively construed the Act otherwise. It bears repeating that both *Prima Paint* and *Moses H. Cone* involved Federal-court litigation. The applicability of the FAA to state-court proceedings was simply not before the Court in either case. Justice Black would surely be surprised to find either the majority opinion or his dissent in *Prima Paint* cited by the Court today, as both are, ante, at 11, 12. His dissent took pains to point out:

"'The Court here does not hold . . . that the body of Federal substantive law created by Federal judges under the Arbitration Act is required to be applied by state courts. A holding to that effect-which the Court seems to leave up in the air would flout the intention of the framers of the Act."

Nothing in the *Prima Paint* majority opinion contradicts this statement.

The *Prima Paint* majority gave full but precise effect to the original congressional intent it recognized that notwithstanding the intervention of *Erie* the FAA's restrictive focus in maritime and interstate contracts permits its application in Federal diversity courts. Today's decision, in contrast, glosses over both the careful crafting of *Prima Paint* and the historical reasons that made *Prima Paint* necessary, and gives the FAA a reach far broader than Congress intended."

Section 2, like the rest of the FAA, should have no application whatsoever in state courts. Assuming, to the contrary that § 2 does create a Federal right that state courts must enforce, state courts should nonetheless be allowed, at least in the first instance, to fashion their own procedures for enforcing the right. Unfortunately, the Court seems to direct that the arbitration clause at issue here must be specifically enforced; apparently no other means of enforcement is permissible.

It is settled that a state court must honor federally created rights and that it may not unreasonably undermine them by invoking contrary local procedure. "[T]he assertion of Federal rights, when plainly and reasonably made, is not to be defeated under the name of local practice." *Brown* v *Western A. Co. of Alabama*, 338 U.S. 294,299 (1949). But absent specific direction from Congress the state courts have always been permitted to apply their own reasonable procedures when enforcing Federal rights. Before we undertake to read a set of complex and mandatory procedures into § 2's brief and general language, we should at a minimum allow state courts and legislatures a chance to develop their own method for enforcing the new Federal rights. Some might choose to award compensatory or punitive damages for the violation of an arbitration agreement; some might award litigation costs to the party who remained willing to arbitrate; some might affirm the "validity and enforceability" of arbitration agreements in other ways. Any of these approaches could vindicate § 2 rights in a manner fully consonant with the language and background of that provision.

The unelaborated terms of § 2 certainly invite flexible enforcement. At common law many jurisdictions were hostile to arbitration agreements. *Kulukundis Shipping Co.* v. *Amtorg Trading Corp.*, 126 F. 2d 978, 982–984 (CA2 1942). That hostility was reflected in two different doctrines: "revocability," which allowed parties to repudiate arbitration agreements at any time before the arbitrator's award was made and "invalidity" or "enforceability," equivalent rules that flatly denied any remedy for the failure to honor an arbitration agreement. In contrast, common-law jurisdiction that enforced arbitration agreements did so in at least three different ways through actions for damages, actions for specific enforcement, or by enforcing sanctions imposed by trade and commercial associations on members who violated arbitration agreements. In 1925 a forum allowing any one of these remedies would have been thought to recognize the "validity and enforceability" of arbitration clauses.

This Court has previously rejected the view that state courts can adequately protect Federal rights only if "such courts in enforcing the Federal right are to be treated as Federal courts and subjected pro hac vice to [federal] limitation . . . ." *Minneapolis & St. Louis R. Co.* v *Bombolis*, 241 U.S. 211, 221 (1916). As explained by Professor Hart:

"The general rule, bottomed deeply in belief in the importance of state control of state judicial procedure, is that Federal law takes the state courts as it finds them. . . . Some differences in remedy and procedure are inescapable if the different governments are to retain a measure of independence in deciding how justice should be administered. If the differences become so conspicuous as to affect advance calculations of outcome, and so to induce an undesirable shopping between forums, the remedy does not lie in the sacrifice of the independence of either government. It lies rather in provision by the Federal government, confident of the justice of its own procedures, of a Federal forum equally accessible to both litigants."

In summary, even were I to accept the majority's reading of § 2, I would disagree with the Court's disposition of this case. After articulating the nature and scope of

the Federal right it discerns in § 2, the Court should remand to the state court, which has acted, heretofore, under a misapprehension of Federal law. The state court should determine, at least in the first instance, what procedures it will follow to vindicate the newly articulated Federal rights. Cf. *Missouri ex rel. Southern R. Co,* v *Mayfield*, 340 U.S. 1,5 (1950).

The Court, ante, at 15–16, rejects the idea of requiring the FAA to be applied only in Federal courts partly out of concern with the problem of forum shopping. The concern is unfounded. Because the FAA makes the Federal courts equally accessible to both parties to a dispute, no forum shopping would be possible even if we gave the FAA a construction faithful to the congressional intent. In controversies involving incomplete diversity of citizenship there is simply no access to Federal court and therefore no possibility of forum shopping. In controversies with complete diversity of citizenship the FAA grants Federal-court access equally to both parties; no party can gain any advantage by forum shopping. Even when the party resisting arbitration initiates an action in state court, the opposing party can invoke FAA § 4 and promptly secure a Federal-court order to compel arbitration. See, e.g., *Moses H. Cone Memorial Hospital* v, *Mercury Construction Corp.*, 460 U.S. 1 (1983).

Ironically, the FAA was passed specifically to rectify forum shopping problems created by this Court's decision in *Swift* v *Tyson*, 16 Pet. (1842). By 1925 several major commercial States had passed state arbitration laws, but the Federal courts refused to enforce those laws in diversity cases. The drafters of the FAA might have anticipated Bernhardt by legislation and required Federal diversity courts to adopt the arbitration law of the State in which they sat. But they deliberately chose a different approach. As was pointed out at congressional hearings, an additional goal of the Act was to make arbitration agreements enforceable even in Federal courts located in a States that had no arbitration law. The drafters' plan for maintaining reasonable harmony between state and Federal practices was not to bludgeon States into compliance, but rather to adopt a uniform Federal law, patterned after New York's path-breaking state statue, and simultaneously to press for passage of coordinated state legislation. The key language of the Uniform Act for Commercial Arbitration was, accordingly, identical to that in § 2 of the FAA.

In Summary, forum shopping concerns in connection with the FAA are a distraction that does not withstand scrutiny. The Court ignores the drafters' carefully devised plan for dealing with those problems. V.

Today's decision adds yet another chapter to the FAA's already colorful history. In 1842 this Court's ruling in *Swift* v. *Tyson*, supra, set up a major obstacle to the enforcement of state arbitration laws in Federal diversity courts. In 1925 Congress sought to rectify the problem by enacting the FAA; the intent was to create uniform law binding only in the Federal courts. In *Erie R. Co.* v. *Thomkins,* 304 U.S. 64 (1938), and then in *Bernhart Polygraphic Co.,* 350 U.S. 198 (1956), this Court significantly curtailed Federal power. In 1967 our decision in Prima Paint upheld the application of the FAA in a Federal-court proceeding as a valid exercise of Congress' Commerce Clause and admiralty powers. Today the Court discovers a Federal right in FAA § 2 that the state courts must enforce. Apparently confident that state courts are not competent to devise their own procedures for protecting the newly discovered Federal right, the Court summarily prescribes a specific procedure, found nowhere in § 2 or its common-law origins, that the state courts are to follow.

Today's decision is unfaithful to congressional intent, unnecessary, and, in light of the FAA's antecedents and the intervening contraction of Federal power, inexplicable. Although arbitration is a worthy alternative to litigation, today's exercise in judicial revisionism goes to far. I respectfully dissent.

In *The Breman* v. *Zapata Off-Shore Co.*, 407 U.S.1, 12 (1972), the Supreme Court noted that the contract fixing a particular forum for resolution of all disputes "was made in arm's-length negotiations by experienced and sophisticated businessmen, and absent some compelling and countervailing reason it should be honored by the parties and enforced by the courts."

A Poultry Growing Contract is not an arm's-length negotiated agreement, quite the contrary, it is a contract of adhesion presented to the grower on a "take it or leave it" basis. Poultry growers are not experienced and sophisticated businessmen.

Although this is true, we must currently recognize that the Supreme Court, whose majority opinion in the Southland case hinged on the term commerce, has spoken and therefore we must accept their decision based on the present law, that arbitration clauses are enforceable in state court actions against all types of business and individuals. Therefore my concern that I am presenting to this committee is that the use of mandatory arbitration clauses along with the waiver of any right to a jury trial is in fact counterproductive to the promotion of the arbitration process. The arbitration process although meant to be expedient and cost effective has become extremely time consuming and expensive under the wording of many of the

mandatory clauses now used in production contracts. Do we want a dispute resolution device or do we want a cost controlling liability reduction device and therefore a income producing element used in the agricultural industry? Do we want to preclude farmers from having any forum to air their disputes, thereby reducing the cost of operations for large companies and supposedly the cost of goods to consumers? What price are we willing to pay for cheaper food? Clearly any waiver of a right to trial by jury must be clear and voluntary. This right is given to criminals, why is it not provided to law abiding, hard working farmers.

Mandatory arbitration clauses are also having an extremely detrimental effect to the reduction of litigation, in that they are creating a totally new area to be litigated, which is in direct conflict with the whole purpose of alternative dispute resolution.

I want to make it perfectly clear that I am not here trying to attack the arbitration process, quite the contrary, I am here to promote it. Although I do not agree that it should be as expansive as our courts have ruled, I have accepted this proposition and will flow with that change. A wise old man told me when I was somewhat younger that change is not painful, resistance to change is painful. Therefore, we must look to find ways to alleviate these problems. I think that there are two simple answers to these complex problems.

—The Federal Arbitration Act can be amended to reflect exactly what courts and entities it applies to.

—The act can also be amended or additional laws passed to mandate that an individual or entity be allowed to choose his forum, whether it be litigation or arbitration, at the time the claim is made.

This is the only time that a knowledgeable and voluntary decision can be made. Just as a yacht is not usable in a five acre farm pond, a john boat is not usable in the ocean. Decisions concerning proper forums have to made after the type, complexity and amount of the claim is known.

We must look to history, for we can't see where we are going unless we know where we have been. This level of concentration in agriculture was experienced in the early 1900's and arising from those problems was the passage of the Packers and Stockyard Act to protect farmers against corporate concentration. Today we must move to do the same. One move is the protection of producers against mandatory waiver of trial by jury and mandatory arbitration clauses.

I remember, early in Law School, a professor informed me that justice and fairness are not the same thing. He was right, justice is based on the law, fairness is fueled by wisdom. The American Bar Association, The American Medical Association, and The American Arbitration Association on the Commission on Healthcare Dispute Resolution used such wisdom and found as follows:

"In disputes involving patients, binding forms of dispute resolutions should be used only where the parties agree to do so after a dispute arises." This is "the only way to guarantee that the agreement to arbitrate is both knowing and voluntary," it is necessary to ensure "that the parties constitutional and other legal rights are protected."

I whole heartedly agree with this finding and believe that the only way to assure the successful promotion of the arbitration process is to ensure that it is voluntary.

I will conclude by citing to you from the Book of Isaiah. Isaiah was a great religious and political influence during the reign of King Hezekiah, King of Judah, whom he served as chief advisor. Chapter10: 1–2 "Woe to those who make unjust laws, to those who issue oppressive decrees, to deprive the poor of their rights and withhold justice from the oppressed of my people, making widows their prey and robbing the fatherless."

Senator COCHRAN. Thank you, Mr. Butler.

Mr. Carlson, President of the North Dakota's Farmers Union. You may proceed.

Senator DORGAN. Mr. Chairman, let me welcome Mr. Carlson. Mr. Carlson is not only president of the Farmers Union, but it's a strong national voice for family farmers and active nationally for a long, long while on these issues. And I welcome him to the committee.

STATEMENT OF ROBERT CARLSON, PRESIDENT, NORTH DAKOTA FARMERS UNION

Mr. CARLSON. Thank you very much, Senator Dorgan, and I thank you very much, Senator Cochran, for holding this hearing. It's a pleasure to be here and a great opportunity to be here.

Mr. Chairman, I'm going to summarize my testimony rather extensively. You have a written copy, and I will try to just hit some of the high points.

As I understand it, the reason for this committee holding this hearing was to help answer the question, and I may be paraphrasing what you said earlier, Mr. Chairman, but to help answer the question does the increased concentration in the agricultural marketplace result in demands upon this committee for greater appropriations in the field of sport and farmers?

Mr. Chairman, our members, and we are the largest farm organization in the State, would answer that question yes by simple logic. When you have more concentration, you have less competition and farm income is reduced. Therefore our demands on this committee and on this Congress for supplemental farm income is increased.

Now, I grant you it is difficult to quantify that amount in many cases. In one I think we do have some quantification of the cost, and that's in the area of transportation. People have talked to this committee about the food chain. Farmers are the beginning of that food chain, and I would say in many cases in terms of market power certainly they're the weakest link in that food chain.

One of the most powerful links in that food chain is very close to us as farmers, and that's transportation. In North Dakota, more than 80 percent of the grain in our State is shipped out by rail. Yet only three percent of our State's elevators have access to more than one railroad.

In short, North Dakota farmers essentially are captive shippers to either Burlington, Santa Fe Springs, or the other alternative, the Canadian Pacific line to move their commodities to domestic users in export terminals.

The North Dakota Public Service Commission and this is where we have quantification estimates that North Dakota farmers are overcharged $100 million annually due to lack of competition. That is $100 million in today's pathetic grain prices that is made up for, to some degree, by our loan deficiency payments.

So that $100 million that is due to overcharging by railroads in North Dakota is actually transferred from LDPs to the railroads.

You have the Upper Great Plains Transportation Institute at North Coast State University, a very well-respected academic think tank also can quantify the cost to farmers of the lack of competition in the rail business.

Just to illustrate, the Burlington Northern Santa Fe transportation rate per car mile for 52-car unit train from Marmarth, North Dakota, to Minneapolis, Minnesota, was $5.68. The rate per car mile for the same type of train from Creighton, Nebraska, to Minneapolis was $3.17, a 79 percent difference.

Again, the train is similar, and the mileage is very similar. What brings this comparison into focus is the fact that the distance from Mina to Minneapolis is 472 miles on the Burlington Northern line, versus 463 miles on the Creighton to Minneapolis line. And such

disparity in rates show up in unit train great movements to the Pacific northwest in a very, very similar manner.

Clearly the lack of competing railroads leads to higher rates and poorer service to the grain shippers who are captive to one railroad line. Whether there is not competition, there must be regulation, and Congress needs to provide authority for rail regulation in those types of instances.

A second area I'll briefly summarize, Mr. Chairman, is in the identification of food chains. In 1999, Dr. William Heffernan of the University of Missouri identified two food chain businesses or conglomeration of businesses capable of controlling food production from genetic engineering to the grocery store shelf. One of those entities was Cargill Monsanto, a second was ConAgra by itself, and a third Novartis/ADM. Cooperatives which were formed to provide independent alternatives have to compete with these vertically integrated corporations.

Some co-ops have had to form alliances with those chains in order to survive. More alarmingly, some cooperatives have been out muscled by corporate giants, denying farmers a measure of self-control and competition.

Earlier this month, Archer Daniels Midland and Farmland industry completed a deal that gives ADM control of Farmland Grain Elevators across the country. The agreement between ADM and Farmland means ADM will take control of Farmland's 24 grain elevators in a joint venture.

The join venture creates a company, ADM Farmland, Inc., to lease and operate Farmland's grain assets. But despite being called a joint venture, there is little doubt that ADM will be in the operation driver seat when it comes to operations. So the big get bigger and competition lessens.

A third and final area, Mr. Chairman, Mr. Heffernan identified just this year in a study commissioned by the National Farmer's Union rapid growth of concentration in the retail food industry. And let me just pick a couple of highlights from that excellent study.

Major players in food retailing in the United States are Kroger, Albertson's, Wal-Mart, Safeway, and Ahold USA, a Dutch firm. These five supermarket chains account for over 40 percent of retail food sales in the United States. By comparison, the top five retailers counted for only 20 percent of food sales in 1993.

What does that mean to farmers and to farm income? Well, it means that as retailers grow larger through acquisitions and mergers, they develop their own vertically integrated distribution systems that tend to shut out wholesalers, small processors, and smaller retailers.

And what that means is that those of us who have been active in forming value-added cooperatives in North Dakota and elsewhere face barriers to entering products into the marketplace, into the food stores when we do form those, be it a pasta cooperative or meat cooperatives. We need to get shelf space, and when those corporations charge high slotting fees, it's very difficult to do that.

PREPARED STATEMENT

I will conclude, Mr. Chairman, by saying that our organization supports the insertion of a concentration title into the new farm bill. We have about a dozen recommendations that we believe should be a part of that concentration title. I will leave those for you to see in my written testimony and conclude with my sincere thanks to you for holding this hearing.

[The statement follows:]

PREPARED STATEMENT OF ROBERT CARLSON

Mr. Chairman: My name is Robert Carlson. I have a small grains and bison farm near Glenburn, North Dakota. Also, I am president of North Dakota Farmers Union, my state's largest general farm organization.

I appreciate this opportunity to share with you the impact to farmers and ranchers that is occurring due to concentration among agricultural businesses.

One fact is indisputable. There are fewer farmers today than there were 20 years ago, and there are fewer businesses in control of the transportation, processing, and marketing of family farm produced crops and livestock. Big business has merged into fewer and larger companies by choice. Sometimes they do so to gain efficiencies, often they do so to more effectively dominate a market. On the other hand, family-sized farms are not getting bigger by choice. While many food processing businesses are recording record profits, many farmers and ranchers are struggling to get by. Clearly, some measure of the healthy profits being reaped by big business are coming at the expense of our nations' small farms and ranches. The viability of our nation's rural communities and infrastructure is closely linked to the relative financial health of farms and ranches.

TRANSPORTATION

Farmers are the first link in our nation's food system. They provide more than enough crops and livestock to feed our nation. The balance is exported which reduces our nation's trade deficit. In North Dakota, more than 80 percent of the grain is shipped out by rail. Yet only three percent of my state's elevators have access to more than one railroad. In short, North Dakota farmers essentially are captive shippers to either Burlington Northern Sante Fe or Canadian Pacific Soo Line to move their commodities to domestic users and export terminals. The North Dakota Public Service Commission estimates that North Dakota farmers are overcharged $100 million annually due to a lack of competition. The Upper Great Plains Transportation Institute (UGPTI) has studied numerous transportation issues that affect North Dakota farmers. UGPTI found, for example, that BNSF's transportation rate per car mile for a 52-car unit train from Minot, ND to Minneapolis, MN, was $5.68. The rate per car mile for the same type of train from Crete, NE, to Minneapolis was $3.17—a 79 percent difference. What brings this comparison into focus is the fact that the distance from Minot to Minneapolis is 472 miles on BNSF's main line versus 463 miles from Crete to Minneapolis on BNSF's main line through Nebraska.

Such disparity in rates shows up in unit-train grain movements to the Pacific Northwest (PNW). BNSF's rate for grain moving from Devils Lake, ND, to an export terminal in Portland, OR, is considerably higher than for grain shipped from Hastings, NE, to the same terminal even though the distance from Devils Lake is 1,424 as compared to 1,788 miles.

In the 1970s, North Dakota was served by five Class I railroads Northern Pacific, Great Northern, Soo Line, Milwaukee Road, and Chicago Northwestern. One can reasonably assume that five carriers competed for grain shipments. With only two Class I railroads today, farmers are faced with trucking their grain a considerable distance to choose between two railroads. In fact, Soo Line is now part of the larger Canadian Pacific Railroad, while Burlington Northern Sante Fe's 35,000 route miles cover 28 western states and two Canadian provinces. It's worth noting that in Nebraska, where BNSF's rates are lower, Union Pacific operates a high density main line which runs parallel to BNSF. Due to concentration in the rail industry, Union Pacific and BNSF have emerged as the two dominate— and only remaining Class I—western rail giants. Both railroads serve many of the same export facilities, manufacturing regions and transportation gateways, which creates keen competition.

In effect, Burlington Northern Sante Fe is profiting at the expense of North Dakota farmers. At the same time, farmers in my state are put at a competitive disadvantage because lower shipping rates provide Nebraska farmers with a "built-in"

discount which can be used to increase their share of the export market. Without strong competition, railroads take full advantage of their captive shippers. The Surface Transportation Board is set up to consider complaints regarding rates. Often, small shippers and individual farmers are overwhelmed by the expense, time, and resources required to initiate a case to prove a railroad has market dominance. Just recently, BNSF was ready to merge with Canadian National, a transcontinental railroad across Canada, until the U.S. government put a moratorium on mergers. CN already has merged one U.S. railroad—Illinois Central—into its map of route miles. How few railroads will it take before one no longer has to make a case for market dominance?

FOOD CLUSTERS

In the 1950s, there were hundreds of Class I railroads. Today there are but a handful. The old adage that "bigger is better" doesn't apply to increasing concentration in agricultural industries, especially considering the impact to family farm agriculture and rural economies—be it transportation or food clusters.

In 1999, Dr. William Heffernan of the University of Missouri-Colombia, released findings of a study which illustrated how consolidation in the food and agriculture industry had molded hundreds of independent food companies into four or five "food clusters." A few business giants understand well how using their massive economic muscle can squeeze higher rates of return for stockholders at the expense of producers and consumers.

Concentration spawns numerous negative consequences that are felt across rural America, including:

—Harming community development by taking profits back to corporate headquarters instead of investing in the communities in which the goods were produced.

—Eliminating independent producers and other independent businesses, who will not be able to stay in business without agreeing to be linked to "the chains" for access to inputs and marketing.

—Making it more difficult for new businesses to start.

Who are "the chains" in Heffernan's study? Three food chains are capable of controlling food production from genetic engineering to the grocery store shelf: Cargill-Monsanto, ConAgra, and Novartis-ADM. The first two built chains through acquisitions, while Novartis-ADM relies on marketing agreements.

Cooperatives, which were formed to provide independent alternatives, have to compete with these vertically-integrated corporations. Some co-ops have had to form alliances with the chains in order to survive. More alarmingly, some cooperatives have been out-muscled by corporate giants, denying farmers a measure of self control and competition.

Earlier this month, Archer Daniels Midland Co. and Farmland Industries completed a deal that gives ADM control of Farmland grain elevators across the country. The agreement between ADM and Farmland, the largest farmer-owned U.S. cooperative, means ADM will take control of Farmland's 24 grain elevators. The joint venture creates a company, ADM/Farmland Inc., to lease and operate Farmland's grain assets throughout the United States. Despite being called a joint venture, there's little doubt that ADM will be in the driver's seat when it comes to operations. The big get bigger and competition lessens.

Heffernan's study reveals some alarming trends regarding the big business of ownership and control of the. Food system. As the study notes, "The changes are the result of notoriously short-sighted market forces and not the result of public dialogue." Think of the food system as an hour glass with producers at the top and consumers at the bottom. There are millions of producers and many millions of consumers at either end, yet only a handful of chains control the processing bottleneck middle. In the 1980s, economists shared a general agreement that if four firms controlled 40 percent of the market, that market was no longer competitive.

Current information on market control is much harder to come by. Heffernan estimated that four firms control more than 40 percent of the processing of major commodities produced in the Midwest. For example, ConAgra is on the list of the top four processing firms for beef, pork, turkeys and sheep (as well as seafood). At the time of the study, ConAgra slipped to fifth place in broiler production and processing. The data also suggested vertical integration in the food system. Cargill ranks in the top four firms producing animal feed, feeding cattle and processing cattle.

The information doesn't reveal the extent of vertical integration in the food system in the U.S. or the complex web of interactions among the top four firms. Nor does the study attempt to address the global nature of the food system. Cargill has

operations in 70 countries and is a privately held firm. Difficulty in obtaining information about such firms makes it equally difficult to formulate public policy regarding concentration.

"The major concern about concentration in the food system focuses on the control exercised by a handful of firms over decision-making throughout the food system. The question is: Who is able to make decisions about buying and selling products in a marketplace,'" stated Heffernan's report.

In the past, most global grain firms were family-held operations that operated in one or two stages of the food system in a few commodities. Today's food clusters, however, are weaving economic webs that trap farmers and ranchers. ConAgra Fertilizer Company may supply the fertilizer for the crop in the field, then buy the grain through ConAgra Grain Company and arrange for it to be to ConAgra Flour Milling. Chun King, a subsidiary of ConAgra could then use the flour for a product destined for a grocery store shelf. When a few companies can wield such market dominance from one end of the food chain to the other, it stands to reason that ConAgra will act to keep everything all in the corporate family regardless of the impact to family farmers.

Today the system is much more complex, beginning with involvement in biotechnology, extending through production and ending with highly processed food. Through mergers, acquisitions, alliances, joint ventures, contracts, partnerships and agreements, the major chains are assembling "clusters of firms" that control the food system from the gene to the supermarket. Within this emerging system, there will be no markets. There will be no price discovery from the gene, fertilizer, processing and production to the supermarket shelf. The only time the public will know the price is when a product arrives in the supermarket.

"As this system evolves, even the price of the livestock feed and its ingredients, such as corn, will not be known to the public, because like today's broilers the product will not be sold," Heffernan said. In a food chain cluster, the food product is passed along from stage to stage, but ownership never changes. The farmer becomes a grower, providing labor and often some of the capital, but never owning the product as it moves through the food system and never making the major management decisions," according to the study.

Heffernan identified the following rapidly emerging food clusters: Cargill/Monsanto; ConAgra; and Novartis/ADM.

Cargill/Monsanto is a leading biotechnology firm and an established cluster. Cargill has the deep pockets needed to buy its way to the top. In 1998, Cargill moved to acquire the grain merchandizing division of Continental, which would give Cargill alone control of 40 percent of all U.S. corn exports, more than 30 percent of soybean exports and at least 20 percent of wheat exports. Cargill's corporate goal is to double in size every five to seven years.

The goal of getting bigger is shared by ConAgra. Heffernan's study found that it was one of the three largest flour millers in North America, ranked fourth in dry corn milling and produced its own livestock feed. ConAgra ranked third in cattle feeding, third in pork processing and second in cattle slaughtering. ConAgra owns about 100 elevators, 1,000 barges and 2,000 rail cars.

A notable difference between ConAgra and Cargill or ADM is that ConAgra follows the processing of food farther down the food chain, ultimately selling labeled food items that most consumers recognize. Armour, Swift, Butterball, Healthy Choice, Peter Pan Peanut Butter and Hunt's are just a few of the ConAgra labels. ConAgra ranked second behind Phillip Morris as the leading food processor in the U.S.

Novartis/ADM is another food cluster that already dominates the industry. Novartis is a Swiss firm that has agribusiness operations in 50 countries around the world. Novartis focuses on crop protection, chemicals, seed and animal health. Novartis entered a five year, $25 million research agreement with the University of California-Berkeley to study gene-library construction, sequencing and mapping.

A primary reason for the Cenex Harvest States merger was the viewpoint that co-ops need more financial muscle and resources to compete in a world of giants. Such giants, however, have encircled the world with their operations.

More worrisome is that independent farmers will have few options in a global food system in which major management decisions are made by a small core of executives. Heffernan says there is no price discovery for chicken feed, chicks or live broilers, as the food product is owned at these stages by the same food cluster. The same is true for turkeys.

Two recent technologies will speed up the process of vertical integration in the crop sector. The first is biotechnology and the terminator gene that keeps farmers locked into one source of seed. The second is precision farming's global positioning system, which will allow decisions about crop management to be made from a re-

mote location. Farmers face the prospect of becoming "hired hands" who drive tractors for a paycheck. Farmers will still shoulder production risks, but management decisions may be made at computers located in a food chain's office hundreds of miles away.

Heffernan says a system of family farms are an economic engine that fuels the prosperity of rural communities. Large non-local corporations, however, see labor as an input cost to be purchased as cheaply as possible while profits are siphoned from the community. As mentioned earlier, large corporations are becoming larger and their profits follow suit. Family farms and rural communities are experiencing economic decline. There is a connection.

"Increasingly, the major decisions in the food system are being made by an ever-declining number of firms. They are primarily concerned with maximizing their profits," the Heffernan observed. But giving in to food clusters is not inevitable. Consumers and government are asking questions about the control and power of food clusters. More to the point, Heffernan offers this challenge. "The centralized food system that continues to emerge was never voted on by the people of this country, or for that matter, the people of this world. It is the product of deliberate decisions made by a very few powerful human actors. This is not the only system that could emerge. Is it not time to ask some critical questions about our food system and about what is in the best interest of this and future generation?"

RETAIL

Earlier this year, Dr. Heffernan issued the results of a new study which looked carefully at concentration in the food retail industry. Let me excerpt the more telling comments from his study.

"Over the last forty years, the agro/food system in the United States, and in much of the rest of the world, has been in the process of being restructured one commodity sector after another. For instance, change came to the beef sector at the feedlot level. Today 20 feedlots feed 50 percent of the cattle and are directly connected to the four processing firms that control 81 percent of the beef processing either by direct ownership or through formal contracts.

"Over the past couple of years, it has become increasingly clear that the food chain clusters are being extended through the retail stage with such new processing arrangements as "case-ready" products. This final step in the alliance is so powerful that it is further restructuring some of the commodity sectors that began horizontal and vertical integration long before the dairy sector.

"The major players in food retailing in the United States are Kroger, Albertson's, Wal-Mart, Safeway and Ahold USA, a subsidiary of the Dutch firm Royal Ahold. Together these five supermarket chains account for over 40 percent of food retail sales in the United States. By comparison, the top five food retailers accounted for only 20 percent of food sales in 1993. Average market concentration of the four top retailers in individual metropolitan areas around the U.S. stood at 73 percent just a few years ago and there is little indication that it has decreased."

The number one supermarket in US, Kroger Co. based in Ohio, is estimated to receive 10 cents of every dollar spent in supermarkets in this country. According to its 1999 Annual Report, Kroger's "primary financial goal is to increase annual earnings per share by 16–18 percent over the next three years." For the record, in 1997 Albertson's had a 22.2 percent return on equity, while Safeway enjoyed 36 percent return on equity.

North Dakota farmers would be tickled if they could look forward to the same rate of return.

As many retailers are now doing, Kroger has ties back to the production side of the food business. In March 1998, Kroger began to sell case-ready beef and pork products under Kroger's own label, and are processed by Excel, a subsidiary of Cargill. This type of arrangement directly ties these retail stores to the Monsanto/Cargill food chain cluster identified by Dr. Heffernan in 1999. As the study explains, "Wal-Mart, which had virtually non-existent food sales in 1993, is now the second largest food retailer in the US, and is on track to become the largest, with surprisingly strong food sales at its Supercenters. When Wal-Mart entered the supermarket business in the mid-1990s, other stores were wary because of the incredible logistics system and supplier pricing that Wal-Mart brought to the business. More importantly, Wal-Mart's large size and market power causes concern as it integrates backward in the food system by creating relationships with dominant food chain clusters. Wal-Mart is one of the first supermarkets to use case-ready meat in its stores. The first such prepackaged beef came from IBP.

"Wal-Mart is a key player on the global level. In 1997, Wal-Mart made a foray into Germany, buying Wertkauf and Spar Handels hypermarkets, and then headed

west in 1999 to purchase Asda, Britain's third largest-supermarket. Wal-Mart also operates in Argentina, Brazil, Canada, and Mexico, and is involved in joint ventures in China and Korea. Some analysts predict there will be only six or so global food retailers in the near future Wal-Mart and the European firms of Carrefour, Ahold and Tesco (UK) are likely contenders."

Dr. Heffernan has revealed how retailer dominance, or vertical integration, in the food system presents challenges for farmers, processors and distributors. As retailers grow larger through acquisitions and mergers, they develop their own vertically integrated distribution systems that tend to shut out wholesalers, small processors and smaller retailers.

Another challenge for smaller food producers and processors is the retailer fees that many large chains demand. It has been estimated that between 50 and 75 percent of total net profit for large retailers comes from "slotting allowances, advertising fees," and other arrangements which do not represent cash sales of food to consumers. There are a whole range of "trade promotions" that manufacturers pay retailers, including slotting allowances (which are supposed to be for new product entry only), display fees, presentation fees, "pay-to-stay" fees and failure fees.

THE IMPACT TO FARMER-OWNED COOPERATIVES

Farmers are at the mercy of large multinational businesses. One solution is for farmers to vertically integrate farther "up" into the food chain. Farmers have pooled their resources to create value-added cooperatives. Two such cooperatives in North Dakota are process bison and durum. In fact, the durum cooperative, Dakota Growers Pasta Company, has become quite successful.

The power of concentration is moving ominously, but quietly, into the food retail sector. Food retailers are using their massive access to consumers to force suppliers to become lower-cost providers of processed food. The bulk of products produced by Dakota Growers Pasta is for the private label market. Small companies such as Dakota Growers Pasta do not have the resources to buy shelf space in major food retail outlets. Even as a value-added product, pasta and other processed foods are becoming commodities themselves as food retail giants increase their power in the food chain. Also, if such co-ops are bold enough to fully promote their own label, they will no longer be in the business of filling private label orders and without that business volume they will no longer be in business. So even as value-added co-ops are moving up into the food chain, retail market power is allowing a few giants to squeeze more pennies out of the system. Farmers make the investment in a cooperative processing plant, retailers use their immense leverage to lock in the benefits.

Higher energy prices and extremely low corn prices have encouraged farmers to explore forming ethanol manufacturing cooperatives. We all applaud these ventures for creating new uses for agricultural products and increasing farm income. But what happens if corn prices increase or energy prices tumble? These co-op's won't have the deep pockets to survive. It's happened before. The results will bankrupt ethanol co-ops that the ADMs of the world will buy up for little investment. And once again, the big will get bigger at the expense of farm families.

Cooperatives work for their farmer-members. They can't simply go out and buy up the competition to become bigger. Cooperatives were formed to create competition and to be answerable to farmers.

In fact, major food retailers are not concerned about the future viability of American agriculture. They are focused on extracting the maximum profit possible for the benefit of stockholders.

As Dr. Heffernan concluded in his study on retail concentration: "The loss of U.S. farmers makes little difference to transnational corporations, whether they are headquartered in the US as are many of the dominant agro/food processors, or in other countries as are most of the emerging retail firms. They travel the world to find where they can 'source' the product with the least cost and then move the product where it can be sold for the highest price. In many of the poor countries, workers in rural areas receive less than five dollars a day. Health and environmental regulations, if they exist, are rarely enforced so firms can operate with lower costs in these countries. Transnational corporations are experts at reaping the economic benefits of globalization while pushing the economic, social, environmental and other costs onto the public. If regulations in this country are implemented to prevent corporations from shifting costs to the public sector, but nothing is done to prevent them from shifting the cost in other countries, then farmers in this country automatically become high cost producers."

Our nation's consumers and farmers are on the outside looking in when it comes to who really makes decisions about food in this nation. Consumers are frustrated when they know the price of wheat has dropped but a loaf of bread costs the same

or more. Farmers shoulder higher transportation costs to ship their grain to market. Just because rail mergers have left them isolated from competition. (In virtually every other business, from automobiles to Internet book sales, its the buyer who has to pay the freight.) Food is far too valuable to leave its future to a few. Food is life. We have seen what happens when a handful of people control our nation's energy supplies. Imagine what will happen if a few giants will ultimately control food from the field to the checkout line.

RECOMMENDATIONS

The loss of family farms and other independently-owned businesses is not inevitable. The accelerated march toward a totally vertically integrated production system can be turned around with action to strengthen the regulatory system and revitalize independently-owned businesses. Here are a number of promising solutions worth your consideration.

Put ag mergers on hold.—Congress should enact a moratorium on agricultural mergers. Last fall the Senate rejected an amendment calling for an 18-month moratorium on large agricultural mergers involving companies with assets of $100 million acquiring companies with assets of $10 million or more.

Prohibit packer ownership of livestock.—Ownership allows the packer to control supply to manipulate the market so that farmers and ranchers receive less money. Legislation in the last Congress would have limited packer ownership to 14 days prior to slaughter.

Strengthen mandatory price reporting.—Congress should continue oversight of mandatory price reporting legislation. The price reporting bill passed in 1999 was promulgated by USDA this fall and is in effect for 2001. However, questions remain regarding regional reporting. Producers need area-specific information that more accurately reflects regional and state prices.

Report concentration data.—Congress should require USDA to collect concentration information. Currently, the University of Missouri collects information to show the top four firms in many different commodity areas. However, the some vital information is not readily available to the university. USDA is in position to have the best access to the information.

Disclose joint ventures.—The Justice Department (DOJ) and the Federal Trade Commission (FTC) should require firms to submit information on joint ventures and alliances that are between firms above a certain size. In many cases, firms that are participating in joint venture arrangements behave just like firms that have merged. Yet, joint ventures and alliances have not been subject to any scrutiny.

Establish permissible levels of concentration.—Congress should consider enacting a level of concentration that triggers an automatic antitrust violation to make it easier for the Justice Department and the Federal Trade Commission to prevent high levels of concentration.

Disclose merger reasons.—Congress should require the Justice Department and the Federal Trade Commission to detail why mergers subject to antitrust review are okay, if the decision is made not to oppose the merger. This would improve accountability.

Require economic impact statements.—Congress should require an economic impact statement detailing the impact a merger or joint venture will have on farmers and ranchers prior to approval.

Label for country-of-origin.—Congress should enact country-of-origin labeling to allow consumers to know where their food supply is being produced. Country-of-origin legislation was introduced in both the House and Senate in the last Congress. Recent issues regarding foot-and-mouth disease has consumer asking where their food comes from.

Focus research & development to family-sized farms.—Congress should ensure that publicly-funded research benefits family-sized agricultural businesses and their communities. Congress should prohibit the use of rural development grants for the creation of factory farms.

Authorize producer bargaining.—The Senate should enact legislation to authorize contract producers to form collective bargaining units to negotiate with integrators.

Fund Local Market Development.—Congress should consider prioritizing research on local and regional markets as well as research on small business structure as part of the National Research Initiative (NRI). By offering information, training and financial assistance in the forms of grants and loans, communities could foster the formation of food cooperatives and other key small businesses.

Prohibit slotting fees.—Congress should prohibit slotting fees, i.e., the large fees charged to suppliers to put their product on the store shelf. Slotting fees provide windfall profits to retailers and create a barrier for new firms and products.

Authorize interstate shipment.—Allow interstate shipment of state-inspected meat.
Provide Model Contract Legislation.—Enact legislation to enhance fairness and provide producer protection in agricultural production contracts.

Senator COCHRAN. Thank you for your contribution to the hearing and for being here and for the insertions that we will have in the record because of your participation.

We'll now hear from Mr. Peter Carstensen, Associate Dean for Research and Faculty Development at the University of Wisconsin, Madison Law School.

STATEMENT OF PETER C. CARSTENSEN, ASSOCIATE DEAN FOR RESEARCH AND FACULITY DEVELOPMENT, UNIVERSITY OF WISCONSIN-MADISION LAW SCHOOL

Mr. CARSTENSEN. Thank you very much, Mr. Chairman. It's a great honor to be invited to participate in this hearing. I especially appreciate the very kind words of Senator Kohl at the beginning.

I think of myself as a competition law and policy generalist, although in the last 3 years I have become increasingly focused on a number of the problems that we have in agriculture and how competition policy plays out there.

My particular focus today in the statement that I submitted was on the role of the GIPSA, and of regulation given concentration in various agricultural markets.

And earlier testimony last year before both the Senate Ag Committee and the Antitrust Subcommittee, the Judiciary Committee, I've made more general statements about concentration and competition policy.

My full statement proceeds in kind of four steps in recommendations. The first step which you've heard a lot about already has to do with the existence of concentrated markets and the kind of buyer conduct that is taking place within the context of those markets. And I don't need to reiterate the kind of data that you've already heard today.

And the additional examples, Farmland being one, another that concerns me deeply in the dairy area Swiza and Dean are proposing to merge, according to media reports. That would give those two firms combined 30 percent of the fluid milk market in America.

So concentration is spreading out into additional agricultural markets. We've heard some suggestion that concentration is necessary for efficiency. It seems to me it is very, very unlikely that in any of these markets the levels of concentration that we see have any relationship to efficiency in production of goods and services. And so I don't think that the efficiency needs are what drives these kinds of organizations.

We also have changes in conduct, the growth of contracting. I don't want anybody to think that we should be opposed to longer term contracting to other forms of marketing in agriculture, but we do need to have a legal structure then that avoids the new and different risks that are created in the context of those kinds of marketing arrangements.

And, again, you've heard a lot already about the problems of differential pricing, of lack of access, of other contract terms. Some of these terms in the arbitration clauses, et cetera. They're extremely questionable. Confidentiality clauses that keep farmers from shar-

ing information with each other. If we want open and transparent markets, we've got to deal with this.

Right now the context is one which I think of as lawless. We do not have a good legal structure to oversee how these newly emerging and developing markets are created, are managed and supervised.

Here again my particular suggestion to you, typical for a law professor, I suppose, is that law plays a very important role in facilitating fair, efficient, competitive, accessible markets, and that—and I wrote at some length about that. How that, in fairness, especially in concentrated markets can arise. How markets can be exploited, manipulated by strategic conduct.

And the role of law both enforcing competition policy but also in providing other kinds of regulation to achieve fair and equitable treatment of individual participants as well as facilitating the efficient operation of those markets.

The Packers and Stockyards Act is an early example of that kind of legislation. 1921 Congress recognized that disputed antitrust interventions in meat markets there were serious problems. And adopted the PSA with a combined interest in facilitating improved competition, addressing anticompetitive issues as well as the fairness of contracts and the access to the market.

And so we have a congressional policy here, which is my third point, GIPSA has simply failed, and the Department of Agriculture has failed to provide the necessary regulation for the modern contract terms and the essential enforcement of access, fairness, and competition.

I was pleased to hear that they are finally going to do something about hog contracts. I'm personally pretty miffed that a year ago almost last September in Denver, a panel of experts of a variety of different points of view on contracting all agreed that there were at least a few things that could be forbidden by rule because there was no possible justification in terms of market for those.

And Mr. Keith Collins was there and heard us all agree, and I think he was a little surprised. They haven't done a thing to even adopt those basic regulations. And that's, to me, a very serious problem. They have the authority, and they are simply not using it to create the rules that will facilitate the fair market practices, the accessible market practices.

Secondly and closely related, there's a serious problem of lack of enforcement capacity organization and just plain staff. And I think that's pointed out in the GAO study. And it's something that needs to be addressed.

It is something which this subcommittee can address if you can find some resources, and then make sure that they are appropriately used by GIPSA and the Department of Agriculture.

Fourth and something that you've heard raised here already, there are a variety of provisions in agricultural law for fairness in a variety of markets. The PSA doesn't address dairy, doesn't address some of the problems in grain contracting. There are other provisions in the laws that address some of these issues in slightly different ways. I think and you've heard this suggested, using the upcoming farm bill, to create a competition title to focus on reconciling, making more general the rules of competition, facilitating

the markets to create better rules of access, better rules of fairness is a wonderful opportunity to kind of restate the law of agricultural markets.

My statement concludes with some suggestions of where we might go. Basically GIPSA needs better organization so that it can adopt and enforce its rules. It needs more adequate resources. I think you need to facilitate those, the work of developing a competition section of your new upcoming statute.

PREPARED STATEMENT

And I got to say to you, gentlemen, in particular this isn't going to be cheap. It's going to cost money to do it. But it's also going to cost you and your staffs time and attention to pursue and make sure the Department of Agriculture follows up and carries out. Because you guys control the purse strings. You're in a position where I hope that you will invest a little time and effort at that part of it. Thank you very much.

[The statement follows:]

PREPARED STATEMENT OF PETER C. CARSTENSEN

PREFACE

I am a generalist with respect to competition law and policy, having studied a variety of industries and legal issues in the course of my career. This background allows me to place many of the issues concerning competition in agriculture in the broader context of recurring competition policy issues that confront our economy, with its reliance on the marketplace as the primary institution for allocating goods and services.

For the last three years, I have focused a significant part of my attention on the specific competitive issues that confront agricultural markets on both the input and output side.[1] As a result, I have been reading a great deal about these issues from a variety of perspectives as well as learning from many experts in the field. I also bring a modest background in some aspects of these issues. As a government lawyer some 30 years ago, I reviewed the old meat packing consent decree and in the process came to appreciate the context within which Congress crafted the Packers and Stockyards Act. In 1995, I served in Wisconsin on a committee that reviewed and proposed modifications for the regulations governing contracts for vegetables being purchased for canning. I have also done an extensive examination of the grain marketing industry in connection with a study of the famous Chicago Board of Trade decision which is a landmark antitrust case.[2] In addition, my work on the competitive implications of other kinds of vertical distribution arrangements has provided me with relevant background on some of the key issues being considered today.[3] Last September, I was one of six invited academic experts in the U.S. Department of Agriculture's Public Forum on Captive Supplies held in Denver, Colorado.[4] We were asked to evaluate the need to adopt regulations under the Packers and Stockyards Act to deal with concerns about anticompetitive and inequitable treatment of farmers and ranchers who raise beef cattle. In addition, in the past year, I have been an invited witness in hearings before the Senate Agriculture Committee and the Senate Subcommittee on Antitrust, Business Rights and Competition on agricultural competition issues.

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[1] Carstensen, "Concentration and the Destruction of Competition in Agricultural Markets: The Case for Change in Public Policy," 2000 Wis. L. Rev. 531.

[2] Carstensen, "The Content of the Hollow Core of Antitrust: The Chicago Board of Trade Case and the Meaning of the Rule of Reason' in Restraint of Trade Analysis," 15 Research in Law and Economics 1 (1992).

[3] E.g., Carstensen & Dahlson, "Vertical Restraints in Beer Distribution: A Study of the Business and Legal Justifications for Restricting Competition," 1986 Wisconsin Law Review 1; Carstensen, "Legal and Economic Analysis of Vertical Restraints: A Search for Reality or Myth Making," in Issues After A Century of Federal Competition Policy, Wills, Culbertson, Caswell, ed., 95 (1987).

[4] The written statements made at that forum are available at the U.S. Department of Agriculture website: www.usda.gov/gipsa/forum/forumprogram.htm

OVERVIEW

I appreciate the opportunity to testify at this hearing. Congress should be deeply concerned about the implications of the existing concentrated structure and continuing patterns of consolidation in the meat packing industry for the survival and economic well being of the farmers and ranchers who raise livestock. The same issues exist in many other areas of agriculture especially in milk production and processing where there is even less effective regulation despite a number of statutes that seek to establish rights and protections for farmers and ranchers. The focus of this hearing is on the Grain Inspection and Packers and Stockyards Administration (GIPSA) which Congress intended to play a central role in ensuring efficiency, fairness and equal access in meat and grain markets. Yet today, livestock growers face serious problems in marketing their animals as a result of the failure of GIPSA to respond appropriately to the dramatic changes in the structure and buying practices in the industries it oversees.

In 1921, Congress adopted the Packers and Stockyards Act (PSA) to provide a legal structure to govern the relationships between farmers and ranchers raising livestock—especially cattle and hogs—and the stockyards and slaughter houses. At that time, and again today, the buyers were highly concentrated nationally and there were, then and now, even fewer buyers in any specific locality. Congress had three goals in adopting the PSA-eliminating anticompetitive practices in the marketplace, ensuring access to all producers, and providing for fairness in transactions. Congress also recognized that it could not revisit the specifics of conduct on a regular basis and so it authorized the Secretary of Agriculture to adopt rules to implement the broad policy goals of the PSA. GIPSA is the agency within the Department of Agriculture that has the assignment of enforcing the PSA by developing rules and regulations that will further the goals of the statute and then enforcing those regulations through administrative proceedings. Further Congress authorized farmers and ranchers who were victims of violations of the law to bring suits and collect damages.

For very important reasons, both competition and equitable treatment were and are equally important elements of public policy toward market contexts in which there is a great disparity of economic power among the participants. In the long run there is strong connection between equitable treatment of market participants and the overall growth and vitality of the economy. But at any point in time, plausible arguments can be made that the concerns are discrete. As a precursor of this more modern dichotomy, the PSA is striking in its explicit combination of both competition and equity concerns within a single statute.

Some of this country's greatest economic successes come from its effective enforcement of equal economic opportunity without regard to whether there is a clear and immediate relationship to conventional notions of competition. For example, our public capital markets are at the center of the growing global economy, exactly because our law and policy provides real protection for the economic interests of the individual investor.

The present situation for the marketing of livestock involves a substantial proportion of transactions occurring outside the traditional spot market. At the same time, the spot market remains a central price-making mechanism. The resulting interaction between spot and captive sales has produced significant and persistent price differentials for similar grades and quality based on the method of sale and unequal treatment of potential sellers. Such outcomes may, arguably, not involve immediate, obvious anticompetitive consequences for the overall market, but they certainly raise serious questions of fairness and equity among producers. Moreover, data on market transactions reveal a very large disparity in prices paid for similar livestock. This too suggests that the present system is not functioning in an efficient or fair manner.

In the longer term inequitable market conditions can and usually do create additional barriers to the growth and development of economically and socially desirable competition. Concentration both increases the incentives to engage in discriminatory conduct and makes it more likely to have adverse consequences on the competitiveness of the affected markets. Risk and uncertainty are two of the greatest barriers to entry into any market. When there are a few dominant players with the capacity to engage in significant strategic conduct with respect to pricing or access, those firms have a clear incentive to employ that power to enhance uncertainty in order to deter new entry or growth by marginal firms.

As a country we have a long and dishonorable history of market manipulation and exploitation in a range of contexts from cheese, grain and meat to gas, automobiles and securities. An essential role for law and regulation is to constitute the operation of markets so that they function in efficient and neutral ways. Law must police the

conduct of such markets because self-interested parties, especially when power is disproportionately allocated and markets are concentrated, have an inherent conflict of interest.

Sadly, GIPSA and the Department of Agriculture have persistently failed to make effective use of their powers. There are neither appropriate regulations nor effective enforce of the law. As a result, livestock sales have increasingly become lawless. Raw economic power determines who gets access to favorable prices and contract terms. In the long run, the failure to facilitate efficient, accessible and fair markets for livestock will only harm both producers and domestic slaughterhouses. It is also likely to result in higher prices for consumers.

Similar issues increasingly exist in other agricultural businesses. Over the years, Congress has sought to address specific problems by focused legislation. Unfortunately, only a few of these statutes have proven even marginally effective in responding to strategic conduct by buyers of agricultural products. It is time for Congress and the Department of Agriculture to take a broader view of the problems that America's farmers and ranchers face in the modern marketplace. The upcoming revisions of the farm bill provide an opportunity to revise, consolidate, and expand the various statutes intended to provide efficient, fair and accessible markets for agricultural products. Such a project is essential to the maintaining workable, competitive markets for agricultural products of all kinds.

In other contexts from airlines to railroads to electric power to telecommunications, we face similar issues. How to make an effective transition from an old market structure and regulatory system to a workable, competitive market? The predictable and recurrent failures in this process result directly from the failure to recognize that lawless markets are inefficient and unreliable. Markets require carefully planned rules to achieve desirable, efficient performance. Such rules do not replace the market with direct commands rather they facilitate its efficient, fair, and equitable operation. The failures and successes of the past can provide important lessons on how to develop appropriate rules and regulations that reduce or eliminate the harms that come from lawless opportunism.

The goals of fairness, access and efficiency can be achieved in livestock markets. But GIPSA and the Department of Agriculture must be committed to this process. In the past, regrettably, these agencies have lacked the will to protect farmers and ranchers. The appropriations process provides a means for Congress to insist that the agency propose, adopt and enforce effective regulations in a timely manner.

The rest of this statement elaborates on these issues. It first discusses the changes in both the structure and conduct of livestock markets as well as the consequences for producers that result from these changes in a lawless market. Second, it is important to appreciate the significant positive role that law and regulation play in creating and maintaining efficient, competitive, fair and accessible markets. In light of this framework and background, there is a discussion of the failures of GIPSA both to initiate appropriate rule making necessary to achieve the kind of market relationships that Congress had sought and to enforce the existing rules in a meaningful and effective way. Fourth, the Department of Agriculture has a number of other obligations to enforce market facilitation legislation that has not been integrated into an effective overall mission by Congress or within the agency. Finally, there are some recommendations including the suggestion that GIPSA get appropriate funding only if it significantly changes its methods of operation so that it can effectively carry out its obligations of rule making and enforcement.

MARKET STRUCTURE AND THE CHANGING NATURE OF BUYER CONDUCT

National and Regional Concentration is Very Substantial

Studies show that the slaughter industry is highly concentrated and that concentration is substantially greater than it was in 1980. The latest statistics that I have found show that the four largest firms in steer and heifer slaughter did more than 80 percent of that business nationally in 2000.[5] Moreover, one firm, IBP alone did more than 32 percent. In hogs the concentration is lower with the four largest firms account for 56 percent of that business nationally.[6] This data understates concentration from the perspective of livestock raisers. Regionally, it is rarely the case that more than two or three of these firms compete as buyers and in many areas effectively only one major firm is buying. Thus, effective concentration in the regional buying markets is much higher. I should also note that the dominant firms in beef are also leaders in pork.

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[5] Cattle Buyers Weekly, September 18, 2000.

[6] Id.

In 1980, by way of contrast, nationally the four largest firms in steers and heifers had 36 percent while the four largest in hogs had a 34 percent share. A significant factor in this structural change was a series of mergers that took place in the mid and late 1980s. At the time of those mergers, the prevailing theory was that if the downstream, consumer markets remained competitive that competition would protect the upstream producers from discriminatory and exploitative pricing by the meat packers. This prediction has proven false. Regardless of the level of downstream competition, a dominant buyer can force down the prices it pays below a competitive price and so extract monopoly rents even though it sells its products in a more competitive market. Recent data on margins in meat packing show that the margin retained by the slaughter houses has increased substantially. This suggests that the slaughter houses are exploiting more vigorously their monopsonistic or oligopsonistic power to depress farm prices relative to the prices they are getting from the grocery stores.

Some have argued that high concentration is necessary for significant efficiency gains. The fact is that high concentration is not related to efficiency. The optimal plants for hog or beef processing require only 2 to 4 percent of the total national volume. If there were some further efficiency from multi-plant operation, something which even industry representatives declined to claim last year in Denver, the market could easily sustain 7 to 10 separate processors in both pork and beef and each could have 2 or 3 plants. This in turn would create a much more competitive buying structure for cattle and hogs.

Because of bad theory in the 1980s we have excessive concentration in meat processing markets today. This means that the packers have both the capacity and the incentive to engage in strategic conduct whose primary function is either to exploit their buyer power or entrench that power against potential competition. This set of factors in turn creates the need for effective regulation of market conduct to reduce the negative impacts of such strategic conduct.

The problems of concentration exist in other important processor markets as well. A handful of firms lead by Kraft dominant cheese making. Today the country faces the threat of similar concentration in fluid milk. The two largest processors, Dean and Suiza, propose to merge. The media reports indicate that between them they may process more than 30 percent of the milk sold in this country. Moreover, these are the only two firms with nearly national processing capacity. As the grocery business consolidates into fewer and fewer national chains, those chains are looking for single suppliers to all or most of their stores. The pending merger will eliminate the potential for vigorous competition in supplying this need which in turn is very likely to harm both milk producers and consumers.[7]

Changes in the Methods of Buying Livestock

Historically, cattle were sold in stockyards in which buyers and sellers met. The livestock were then sent onto nearby slaughter houses. The stockyard provided the advantage of an open auction market. Unfortunately, because of the limits imposed by geography, only a few slaughter houses could operate in close proximity to any specific stockyard. The result was rampant market manipulation. This experience is an important background to the PSA which sought to regulate the conduct of stockyards to ensure, insofar as law could, that they operated in an open and fair way, accessible to all.

With the development of refrigerator trucks and the interstate highway system, slaughter houses moved into the country to be closer to the sources of supply. This produced a different context in which buyers from the various slaughter houses visited farmers and made bids on livestock. As a youth and young man I recall hearing my beef raising cousins in Iowa discuss the pros and cons of different pricing methods and the qualities of the buyers for the four or five different slaughter houses that were regular bidders for their steers.

As the packing industry consolidated in the 1980s and 1990s the number of bidders declined to one or two. Increasingly, favored feedlot operators were offered contracts of one kind or another to supply cattle or hogs to specific buyers. Today, most livestock is sold under some kind of a longer term contract arrangement usually with the price based on a reported market price at the time of actual delivery. This creates a strong incentive for price manipulation. If a buyer can lower the public price, that will lower its costs over a much larger number of purchases. Moreover, because contracts require delivery within set time periods and the packer has a

[7]A recent study of milk pricing in New England suggests that after Suiza acquired dominance in that region it played a leading role in increasing the margins between the farmer and consumer. Cotterill, R.W., and A. W. Franklin. "The Public Interest and Private Economic Power: A Case Study of the Northeast Dairy Compact," May 3, 2001.

greater ability to manage its public auction demand to control the prices it pays on contract.

Interestingly, in the cattle business, despite these incentives the contract producer gets the advantage of persistently higher prices in comparison to direct sale prices. This is the repeated finding of major studies sponsored by GIPSA. This does not disprove the claim that prices are manipulated to achieve, on average, lower prices than a robustly competitive market would have produced. It only establishes that the packers as buyers have persistently favored some producers over others.

The point here is that there are persistent price differences for similar grade and quality livestock based on the method of purchase. Moreover, and equally important, the packers determine which producers get the benefit of the higher contract prices. The implication is twofold. First, the favored operator has an incentive to serve its economic master because its next best option involves a substantial loss of revenue. Such an operator is not well positioned to bargain effectively on the terms of the transaction. Second, the fact that the buyers are under no obligation to deal with all comers on equal terms means that they can refuse to deal with operator. The fact of high concentration on the packers side means that such refusals will often deny access to the more lucrative contract market. Indeed, by refusing even to bid for livestock for immediate sale the packer can eliminate a disfavored operator from the business entirely.

Such bargaining power with its capacity to force terms on the seller or even destroy a farmer's business by refusing to deal entirely is exactly the kind of discretion that the PSA was supposed to regulate to ensure both fairness and equal access for farmers and ranchers.

As the more comprehensive price reporting of sales has become available, a further and equally significant fact is emerging. On sales of similar livestock prices vary quite substantially. This again suggests that the markets are working very imperfectly. Why such price differences exist and persist should be source of great concern to those charged with ensuring the fairness and openness of these markets.

The most extreme example of what can happen is found in poultry. Once there was an open market in which growers could sell their chickens and turkeys. Today, there is no longer a spot or public market for general production. All supplies are captive under contracts that impose a wide variety of unfair conditions on the growers. Recently, the attorney general of Oklahoma has offered the opinion that many contracts for production of crops and livestock are now contracts of adhesion which may in fact reduce independent farmers to the position of employees.[8]

Without regulation, the risk is that the public markets will either disappear entirely or that they will become very vulnerable to manipulation. These risks impose burdens and costs on farmers and ranchers as well as consumers. In the long run, such market contexts are inefficient, anticompetitive and undesirable for all those who rely on such markets to move food and fiber from the farm to the consumer.

THE CONSEQUENCES OF A LAWLESS MARKET: STRATEGIC CONDUCT, DENIAL OF ACCESS, UNFAIR CONTRACTS

Among the earliest antitrust cases were ones that challenged the legality of regulations governing stock yards.[9] In the two initial cases, the Supreme Court upheld the restrictions because it interpreted them as designed to avoid conflicts and opportunistic behavior that undermine the creditability and viability of the stockyards in question. Thus, from the earliest judicial review, the courts have recognized that restrictions on some kinds of conduct are essential to the fair and efficient operation of trading markets. Thus some restraint on conduct by market participants would be acceptable in the face of the Sherman Act's condemnation of contracts in restraint of trade.

On the other side of the leger, in 1912, the Court upheld a criminal complaint against an individual who sought to manipulate a commodity exchange.[10] In that same era, the government sued both the egg and butter exchanges because in each case dominant buyers were manipulating the pricing process in order to influence the prices of off-exchange transactions.[11] These three cases underscored the inherent risks to the market that arise when thin spot markets play a central role in the process of bringing goods, especially agricultural products, to consumers. The management of public price making has remained a continuing source of concern

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[8] Oklahoma Attorney General Opinions 01–17 (April 11, 2001).

[9] Anderson v. U.S., 171 U.S. 604 (1898); Hopkins v. U.S., 171 U.S. 678 (1898).

[10] U.S. v. Patten, 226 U.S. 525 (1912) (the case involved the cotton exchange, but Patten was also a major grain trader).

[11] U.S. v. Chicago Butter & Egg Board, (Civil 30042, N.D. Ill. 1910); U.S. v. Elgin Board of Trade (Eq. 31051, N.D. Ill. 1912).

to antitrust law in a wide range of fields exactly because of its potential to be used in a variety of anticompetitive ways.

In 1913, the government challenged the over-night pricing rules for grain to arrive of the Chicago Board of Trade. The Board of Trade ultimately won in the Supreme Court in 1918 despite the undisputed fact that these rules operated to establish rigid overnight prices that all members had to pay.[12] The record showed that this rule was necessary so that the Board could provide an efficient, open, and non-discriminatory market for grain. Prior to the rules, large integrated firms were able to manipulate the market at various times by bidding off the exchange at night at higher prices than they were paying on the exchange. In addition, the Board of Trade changed its rules for bidding to rural elevators so that the integrated firms were no long able to discriminate among sellers of similar grades of grain. The impact of these rules was to make the commodity exchange a more efficient and effective market for grain despite the constraints imposed on some of its members freedom of action.[13] Such constraints are essential in any organized exchange market. Participants, particularly those who are fully or partially integrated, have a strong incentive to behave in opportunistic ways with respect to their participation in the organized market. Such conduct must be restricted if organized exchanges are to provide effective and reliable price making mechanisms.

Two other leading Supreme Court cases also involved market manipulation activities that bear some relationship to the current situation in livestock and agriculture generally. In the Socony case,[14] the major oil refiners conspired, unlawfully, to buy up surplus gas to affect the spot market price and manipulated the reporting of prices in order to ensure higher prices to themselves under their long term supply contracts with wholesalers and distributors. These long term contracts used the spot market price to price specific deliveries. Lastly in American Tobacco the dominant cigarette makers were found to have violated the Sherman Act by collectively biding up the price for tobacco that was useful to their competitors but not to themselves.[15] By manipulating the tobacco auctions, they caused their competitors to have higher input costs which disabled their competition. Thus, in the latter case, the goal was to harm competitors while in the first case it was to impose higher costs on customers. The most relevant point for present purposes is that in both cases auction or spot market manipulation advanced anticompetitive goals. The highly concentrated character of the gasoline refining and cigarette production markets meant that those firms had both the incentive and the capacity to engage in market manipulation to advance their anticompetitive interests.

In two decisions in the course of the 1990s the Supreme Court has reiterated its recognition of the risks to competition and economic welfare arising from vertical restraints.[16] These cases involved distribution restraints and the Court's concern was with the power created in retailers by exclusive territories and similar restrictions on intra-brand competition to over charge their customers. Nonetheless, these decisions recognize the broader truth that vertical restrictions of every kind, however laudable their initial intent, can have adverse competitive effects. In another important decision the Court recognized that a refusal to deal with a supplier based on an understanding with another supplier can constitute an unreasonable restraint of trade.[17] The lesson once again is that upstream vertical agreements can also result in serious harm to the competitive viability of the market system.

Recently, the Seventh Circuit Court of Appeals, following up on this theme, upheld the Federal Trade Commission's challenge to Toys R Us (TRU), a major toy retailer, efforts to restrict its suppliers sale of toys to TRU's competitors.[18] TRU is the largest retailer of toys in the country—selling about 20 percent. It induced its major suppliers to refuse to provide comparable toys to its lowest price competitors in order to protect its profit margins. There is a somewhat similar case in the European Union involving retailer buying power.[19] These cases re-emphasize the dangers

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[12] Bd. of Trade of the City of Chicago v. U.S., 296 U.S. 231 (1918). This decision is the leading decision applying the rule of reason to a restraint of trade and upholding it.

[13] For a fuller discussion of the business and economic factors in the board of trade case see Carstensen, supra note 2.

[14] U.S. v. Socony Oil Co., 310 U.S. 50 (1940).

[15] U.S. v. American Tobacco, 328 U.S. 781 (1946).

[16] Atlantic Richfield Co. v. USA Petroleum, 495 U.S. 328 (1990); State Oil v. Khan, 522 U.S. 53 (1997).

[17] NYNEX v. Discon, 525 U.S. 128 (1998).

[18] Toys R Us v. FTC, 221 F3rd 1334 (7th Cir., 2000)

[19] Kesko/Tuko, Case T–134197, European Commission; see, Curtin, Goldberg, Savrin, "The EC's Rejection of the Kesko/Tuko Merger: Leading the Way to the Application of a "Gatekeeper" Analysis of Retailer Market Power Under U.S. Antitrust Law," 40 Boston College L. Rev. 537 (1999).

of buying power to the overall competitive operation of the market. They also show that lower market shares may create serious competitive issues than are normally seen on the selling side. Congressional hearings on the effect of slotting allowances have highlighted comparable harms to competition in the food distribution system.

Outside the courts, Professor Willard Mueller and associates have examined the operation of the Wisconsin cheese exchange and found that it was manipulated under certain conditions to the advantage of the major buyers. The underlying facts are similar to the manipulation of cheese exchanges by the meat packers at the turn of the century. Moreover, this study shows how major buyers have the incentive to seek to use commodity trading to protect their long run economic interests in controlling price. Recently, the 9th Circuit has upheld the right of dairy farmers in California to sue the cheese makers for the reduced milk prices that resulted from this conduct.[20] As I discussed earlier the pending Suiza-Dean merger will move fluid milk markets toward the structure of beef and cheese markets to the detriment of producers and consumers alike.

The upshot of this record is that when markets are concentrated, dominant firms have great incentives to engage in anticompetitive discriminatory conduct whose purpose is both to entrench and exploit their position.

LAW AND REGULATION AS A POSITIVE FORCE IN FACILITATING EFFICIENT, COMPETITIVE, FAIR AND ACCESSIBLE MARKETS

Public policy in this country employs two strategies to accomplish the goals of fair, efficient and accessible competitive markets. First, antitrust law exists to maintain competitive market structures and forbid anticompetitive conduct. Second, industry and topic specific legislation seeks to provide a balance between the interests of contending groups of economic actors. Such legislation seeks fairness and equity in the market place.

Competition and fairness tend to yield similar results. In the case of regulating concentrated markets, however, there is some tension. To induce competitive efforts among existing dominant firms, it is sometimes the case that concealing information and creating opaque market situations will induce such firms to behave in a more competitive way. Conversely, creating greater price transparency is likely to facilitate tacit coordination among dominate firms provided substantial barriers to entry remain. On the other hand, reducing the capacity of dominant firms to engage in opportunistic, strategic behavior with respect to key inputs through regulating the manner in which the market for inputs operates provides the kind of assurance that new entrants or marginal firms seeking to expand need to encourage more active competition on the merits.

I reference these tensions to underscore the complexity of the choices that must be made and necessity that there be a reasonable comprehension of the dynamics of the specific markets including the potential for effective entry and expansion.

Because antitrust law is concerned with competition and not the specific interest of traders in equitable treatment, Congress and the states have created a number of specific statutory systems to protect the less powerful parties in their relationships with powerful customers or suppliers. At the national level there is specific legislation to protect the interests of automobile dealers,[21] gas station operators,[22] as well as investors in the stock market.[23] State law provides protection for independent dealers serving major enterprises.[24] The central theme of all of these regulations is the need to ensure equitable treatment of all those who participate in an economic process. Because there are substantial disparities in economic size and power in a wide range of markets, government has necessarily had to play an important role in ensuring the equitable treatment of participants.

In agricultural markets in particular there is a long history, dating back to the earliest days of the English common law, of concern for the equitable treatment of producers and consumers. That history shows that there have been frequent abuses of temporary market dominance and unacceptable efforts to exploit informational or strategic advantage. Some of the remedies attempted in the past proved equally unattractive. Hence, the lesson is that there is a long standing and significant concern for the fairness and equity of markets in agricultural products. This concern is also evidence that over the long sweep of history there have been recurrent examples of strategic behavior causing serious social dislocation and requiring legislative or administrative intervention.

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[20] Knevelbaard Dairies v. Kraft Foods, 232 F3d 979 (9th cir. 2000).
[21] Automobile Dealers Day in Court Act, 15 U.S.C. 1221 et seq.
[22] Petroleum Marketing Practices Act, as amended, 15 U.S.C. 2801 et seq.
[23] Securities and Exchange Act of 1934, as amended, 15 U.S.C. 78a et seq.
[24] See, e.g., Wisconsin Fair Dealership Law, Wisc. Stat. chap. 135.

Modern regulation of market equity involves two general kinds of concerns both of which are manifest in the present problems facing American agriculture. One concern is for the integrity of the transactional market when it plays a central role in defining the price of transactions as well as equal treatment of participants in terms of access to favorable opportunities to buy or sell. This is most evident in the rules governing access to public securities markets in which all traders are to receive as equal treatment as possible. In addition, the law demands extensive and continuous disclosure of detailed business information so that investors and their advisors can make informed judgements.

A second recurring concern in the law is for equitable terms with respect to long term contractual arrangements. The petroleum marketing act, for example, gives the lessee of a gas station the right, under certain circumstances, to buy the station if the refiner proposes to sell it to a third party. The fundamental concept here is that the law must protect the interests of powerless actors in the market in the interest of both equity and efficient market operation.

The present situation with respect to captive supplies of livestock and their impact on the spot market as well as the implication of foreclosing substantial numbers of growers from access to longer term contracts illustrates the combined problem of equity and access. If foreclosing certain forms of transaction creates any real economic problems for the packers, then the question is how can any legitimate needs be satisfied in a way that is consistent with the fundamental goals of equal access and equitable treatment. A useful starting point might be the suggestions of Professor Stephan Koontz (Colorado State) to the Senate Agriculture Committee last year concerning livestock markets. Professor Koontz suggested that the Department of Agriculture needs to be much more pro-active in developing new grading standards and certification systems so that the transactional market could provide a place in which buyers could readily find the kind and quality of animal that they sought.[25] It is not enough he points out to be concerned with bad practices, the government must be take the initiative to modernize the spot market and related market transactions to facilitate the desired transactions. This point applies generally. Government must take the initiative to facilitate workably competitive, efficient market contexts. Public markets do not happen on their own in equitable and fair ways. The strength of the economic interests at stake in the market will shape them to serve their own interests. The role of government is to restore the balance and facilitate the equitable development of the market.

As one who has looked askance generally at conduct oriented regulation, I would say that my own first preference would be to see a large scale restructuring of the meat packing industry. The number of plants of the largest scale substantially exceed the number of firms; yet such levels of multi-plant operation are extremely unlikely to achieve any notable economies.[26] Indeed, the coordination costs are likely to result in slightly higher overall costs for such extended networks. If the industry were reorganized to make it more workably competitive, e.g., limiting firms to no more than 3 or 4 plants in dispersed parts of the country, there would be much more reason to have confidence that observed market behavior was efficiency oriented and not infected with anticompetitive or strategic considerations. In such a world, specific conduct regulations would be less necessary except, perhaps, for a requirement of open access to long term contracts. In fact, in my view, as I have written in connection with the somewhat analogous language of the FTC act, sections 202(a) and 202(e) give the secretary the authority to impose such requirements on the industry.[27] However, in the case of the PSA, the secretary would have to find that purely conduct oriented rules would not be effective. There are a few antitrust cases involving restraints of trade where structural relief was imposed that would provide further support for such an approach.[28]

Realistically, of course, it is unlikely that the secretary would at this time adopt regulations that required large scale reorganization of the meat packing industry, however desirable that might be. Hence, the focus has to be on the role of law to minimize or eliminate the unfair, strategic, inefficient conduct of powerful buyers. In a lawless market, economic power is unchecked. That which is rational for individual, powerful economic actors is not necessarily fair to the parties on the other

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[25] See statement of Professor Koontz to the Senate Agriculture Committee at its hearing on April 27, 2000.

[26] This point was made recently by James MacDonald, a senior USDA economist. MacDonald, "Concentration in Agriculture," paper presented at the Agriculture Outlook Forum, Feb. 24, 2000, at p.3.

[27] Carstensen & Questal, The Use of Section 5 of the Federal Trade Commission Act to Attack Large Conglomerate Mergers," 63 Cornell Law Review 841 (1978).

[28] U.S. v. Paramount Pictures, 334 U.S. 131 (1948); see also U.S. v. American Can Co., 87 F. Supp. 18 (N.D. Cal. 1949).

side of the transaction or, more importantly, in the best long run interest of economic efficiency.

The commands of the Packers and Stockyards Act (PSA) are as concerned with controlling the unfair conduct of packers as they are with the elimination of purely anticompetitive conduct in the market. As such, the PSA is the precursor of a number of statutes at both the national and state levels that seek to redress the balance between small business operators and their large customers or suppliers. Thus, section 202(a) of the PSA forbids packers from using "any unfair, unjustly discriminatory, or deceptive practice or device" without requiring that such practice or device also have an anticompetitive effect or intention. Similarly, section 202(e) condemns "any course of business" which has "the purpose" or "effect of manipulating or controlling prices" as well as such acts when they cause monopoly or restrain competition in the market. Other provisions, e.g., sec. 202(c), explicitly require adverse competitive effect before there is a violation. Thus, the PSA is a blend of provisions controlling conduct based on considerations of fairness and equity and ones focused on avoiding broader anticompetitive effects.

The PSA has a clear point of view—it instructs the Secretary to regulate the conduct of packers and stockyards to protect producers and buyers from unfair and discriminatory conduct. PSA 202(a) and 202(e) are clear that equity and fairness concerns in addition to overall competitive analysis are relevant to evaluating such conduct. Moreover, the PSA recognizes that harmful results can be either intended or the consequences of the decisions made by packers. Thus, that the packer did not intend to discriminate or be "unfair" and indeed did not gain by its conduct is no defense. If the effect of particular market conduct is to discriminate, then there is a violation. This aspect of the PSA necessarily includes a concern for the equitable distribution of wealth as between the various participants in the process of production. This is an important theme in public regulation of market activity.[29]

The PSA does not confer price regulatory power on the Secretary. Rather the Secretary's role is to ensure equal and fair treatment of those who supply and buy from meat packers as well as to enforce competitive market requirements on the conduct of the packers. Legal regulation is essential to the creditability of any public market because of the incentives of powerful firms engaged in the market to exploit their strategic advantage to the detriment of the public users of the market. Federal securities law which strictly regulates the operation of our public capital markets is a good example of this strategy. American investor protection laws are so valuable that foreign corporations voluntarily list on our stock exchanges so that their shareholders will get the benefit of American securities law including full disclosure of corporate information. This strategy in turn permits easier and cheaper access to the public capital market because investors have the protections of a strong regulatory system ensuring equitable treatment.

Unfortunately the authority of the secretary to police the fairness and equity of treatment in agricultural markets is limited. The PSA addresses only the business of meat packing. No comparable direct authority exists to policy grain or dairy contracts. As market structure and conduct akin to that in livestock and poultry markets come to dominate other sectors, it will be increasingly important that the law authorize the Secretary to provide rules and regulations to ensure fairness in pricing and equal access to market opportunities for all farmers and ranchers.

THE CURRENT PROBLEMS WITH GIPSA

There is a manifest need for effective regulation of the livestock markets to ensure efficiency, fairness and equity in light of the high concentration and resulting incentives to engage in strategic conduct. The public record fully documents the existence of serious problems concerning both fairness and equity in these markets. To remedy these problems, two elements are essential. First, there need to be rules to define the scope of bargains and provide rights of access to the market place. Second, those rules need to be enforced effectively by a combination of agency action and private claims when necessary.

Given the dramatic changes in the ways in which livestock are sold, it is striking that the Department and GIPSA have totally failed to exercise the rule making authority that they possess to craft appropriate, market facilitating regulations to govern the new methods of buying and selling livestock. The previous administration failed for years to act on a petition from the Western Organization of Resources Councils (WORC) that requested new regulation of contract buying of livestock. I

[29] See Calabarsi & Melamed, "Property Rules, Liability Rules and Inalienability: One View of the Cathedral," 85 Harv. L. Rev. 1089 (1972) (analysis of economic regulation stressing the role and effect of law in creating and assigning rights to wealth).

am not here endorsing the WORC proposal in its entirety. It did point to central issues in the emerging market for cattle and the record showed beyond any reasonable dispute that there were and are problems with the present operation of that market. What is intensely frustrating is that the previous administration never acted one way or the other on any element of the proposal even those as to which there was nearly unanimous consensus.

Specifically, at the USDA's forum last September in Denver on the WORC proposal, the panel of experts who did not agree on much else were in agreement that packers should never be permitted to use as the basis for pricing a future delivery their own price for cattle on the day of delivery. Such a method of pricing was unduly vulnerable to manipulation and was unnecessary for any legitimate pricing need. Yet the Department of Agriculture and GIPSA could not bring themselves to adopt even such a basic prophylactic rule!

In sum, the first serious failure of GIPSA under the past administration was its complete failure to develop rules and regulations to govern the emerging market situations. Left to their own devices, the large buyers will, as the Attorney General of Oklahoma has opined, force contracts of adhesion onto farmers and ranchers. For example, such contracts often deny the producer access to the courts and at the same impose unfair and inequitable arbitration terms that effectively deny the producer all recourse. Confidentially clauses keep farmers and ranchers from sharing information that would make them more sophisticated decision makers. Even price reporting is unavailable where buyers are very highly concentrated. This fact would seem to require special regulations to ensure equitable treatment of sellers in such markets. Yet GIPSA has done and is apparently doing nothing to provide basic regulation for any market.

Market facilitating regulation is long over due and this committee should insist that GIPSA get on with the task. The courts have had and will continue to have a very hard time interpreting the general terms of the PSA. They can not protect farmers and provide appropriate balance without regulations that better define the rights and duties of the parties.

The second failure of the Department of Agriculture is its refusal to staff GIPSA in a way that would permit effective enforcement of current regulations let alone the ones that ought to be adopted. In September 2000, the GAO reported on GIPSA to Congress.[30] That report highlighted the continued failure of GIPSA to enforce effectively the existing regulations. The report highlighted the very poor structure and staffing of investigations. GIPSA itself lacks the staff and authority to pursue the cases it investigates. Indeed, it appears the staff must investigate without the support and involvement of those who will litigate the case if it is filed. Moreover, the number of attorneys available in the general counsel's office to conduct litigation has declined in recent years to a pitiful five—not all of whom are assigned full-time to GIPSA.[31] The report further indicates that GIPSA did not have appropriate methods for investigating "complex anticompetitive practice[s]".[32]

Regulations, however good, have little effect if there is no enforcement. While farmers and ranchers can bring individual cases or class actions, such efforts are very time consuming and may focus more on specific private concerns and less on the broad public interest in ensuring open and fair markets. Thus, effective public law enforcement is essential to the creation and maintenance of fair and open markets. This is the lesson of antitrust law and securities law to name but two examples.

THE BROADER MARKET FACILITATION OBLIGATIONS OF THE DEPARTMENT OF AGRICULTURE

The PSA is not the only statute that addresses issues of competition and access in agricultural markets. The Agricultural Fair Practices Act deals with specific kinds of unfair trade practices involving coercion of producers into joining or not joining associations.[33] The Capper Volstead Act not only exempts agricultural cooperatives from antitrust law in some significant degree but also requires the Secretary to police market conduct to ensure that cooperatives do not unduly restrain competition.[34] There are a number of other examples. The common theme is that Congress has identified specific failures of these markets to operate in fair, accessible and efficient ways and has adopted specific statutory rules. The result is a

[30] GAO, Report to Congressional Committees: Packers and Stockyards Programs Actions Needed to Improve Investigations of Competitive Practices (2000).
[31] Id. 15.
[32] Id. 6.
[33] 7 USC sec. 2301 et seq.
[34] 7 USC sec. 291, 292.

patchwork of responses to particular issues and problems that has not been revised and made systematic to define a workable legal context for agricultural markets.

As Congress has come to rely more on the market place to set prices and allocate demand for supplies in these markets, there is an increased need to review this legislative thicket and identify a systematic set of rules to govern the market process in agriculture. The elements of this system recur in various legislative context and are entirely consistent with the PSA. The goals are efficient, competitive, fair and accessible markets.

I reference this broader context here because Congress is embarking on a major review of agricultural policy as it is considering new general farm legislation. I understand that there is discussion of including a title on competition issues. It seems to me that an important element of that review should be an effort to access the scope, consistency, and operation of the existing complex of laws regulating agricultural markets. It is likely that this would lead to an effort to revise and restate this law in ways that are more applicable to modern conditions and provide for more general coverage for the basic principles found in those laws. Such an effort would also require a focused effort to identify the means for effective enforcement of these regulations through an appropriate combination of public and private mechanisms.

Related to the legislative patchwork governing agricultural markets is the disjointed structure of the Department of Agriculture's own enforcement efforts. GIPSA deals with meat and grain. Another part of the Department deals with cooperatives and still others focus on market information. It appears to me that a full review of the organization of responsibilities for administering the market facilitation aspects of the Department's mission would be an important contribution to modernizing and making effective the implementation of competitive, fair, efficient and accessible agricultural markets.

RECOMMENDATIONS FOR CREATING OR RESTORING A WORKABLE MARKETPLACE

Several matters seem to me to be central to dealing effectively with the need for an efficient, fair, competitive and accessible agricultural marketplace. I have the following recommendations:

—GIPSA and the Department of Agriculture need to address the organizational problems inherent in the present structure of the department. It is not organized in a way that permits it to carry out its obligations to facilitate the working of agricultural markets. This means that both GIPSA's internal operations and its relationship to other market facilitating elements of the department need to be carefully examined and a better system of coordination needs to emerge.

—There is a very specific need to deal with lawless markets in livestock by effective rule making in light of three goals for PSA. Good, market facilitating regulation makes strategic behavior less feasible and serves the long best interest of all participants in an open, accessible, competitive and efficient market. As the nature of market relationships have changed, it is especially important to develop rules and regulations that guide all parties as to their rights and duties. The risks of disruption and distortion in agricultural markets are real and substantial if such rule making is not undertaken in a timely fashion.

—Regulation without effective enforcement of the rules will not resolve the inherent problems of the marketplace. It is essential to implement recommendations on reorganization of staffing of GIPSA so that it can become an effective law enforcement agency.

—More generally, as Congress approaches the process of revising the overall statutory regime governing American agriculture, it is very important to initiate a review of the various statutes that regulate these markets and to develop a comprehensive statutory scheme to facilitate all agricultural markets. The fundamental goals for this system are well established; the challenge is to create a more systematic and workable set of rules that provide structure for the wide range of markets and market contexts in which farmers and ranchers sell their produce.

—Lastly, reform is not cheap. To have agricultural markets that are competitive, efficient, fair and accessible, there are costs. One part is to make sure that the Department of Agriculture has the financial resources to hire the necessary staff. The other and perhaps less visible cost is for Senators and Members of Congress to monitor the progress of the Department to make sure that it in fact carries out its obligations. These costs should be incurred. The alternative is the gradual erosion of our entire agricultural economy.

CONCLUSION

American agriculture in general and in the livestock segment of that industry is at a cross roads. The persistent concentration and radical changes in the methods of buying livestock have created serious problems which are likely to become worse in the absence of necessary market facilitating regulations and effective enforcement of those rules. Not all the problems facing agriculture are going to be solvable by reliance on market. But Congress has wisely elected to seek to rely as much as possible on the market as the best mechanism to organize the movement of food and fiber from the farmer and rancher to the final consumer. Given that fundamental choice, the Department and GIPSA must perform better their assigned tasks of facilitating a competitive and efficient marketplace while also ensuring access and fair terms to producers.

Senator COCHRAN. Thank you, Mr. Carstensen.

Mr. Dan Kelley.

STATEMENT OF DAN KELLEY, FARMER, STATE OF ILLINOIS

Mr. KELLEY. Thank you, Mr. Chairman, Mr. Dorgan. It's a pleasure to be here and an honor to be here. I'm a farmer from Normal, Illinois, where I'm actively engaged in a farming partnership with my two brothers.

In the interest of time and the fact that I still have soybeans to plant, we'll move through this rather quickly. My brothers and I operate a couple of thousand acres of land in central Illinois and also serve as chairman of the board and president of GROWMARK Federated Regional Cooperative located in Bloomington, Illinois.

As a federated cooperative GROWMARK is owned and controlled by some 250,000 independent family farmers, and there are approximately 320 local cooperatives with their total sales being about $1.4 billion.

The farmer owners that make up GROWMARK range in size from part-time hobby farm operators to full-time producers, commercial operations. But the average size is about 300 acres. The mission of GROWMARK when it was started 75 years ago was to improve the long-term profitability of its farmer owners. That purpose still exists today.

As an independent family farmer, I cannot stress just how important that continues to be, especially in today's business environment. Like all farmer cooperatives, GROWMARK has unique accountability and focus because of the fact that it is farmer owned and farmer controlled.

GROWMARK over the last 5 years has returned $140 million in additional income to its members as a result of value added activities in the form of patronage. Farmers today continue to operate in a very challenging business environment. I think that's been addressed by other panelists.

Globalization continues to derive changes throughout every sector of our economy. We're seeing across the board consolidation in energy, chemical, banking, financial services and especially in the food processing retailing sectors.

The National Council for Farmer Cooperatives, the national trade organization representing America's farmer-owned cooperatives which GROWMARK is one recently did an analysis of the relative position of farmer cooperatives in the food and agriculture system.

Some of the items that it highlighted were that while cooperatives continue to play a significant role in the farm economy ac-

counting for 28 percent for all farm supply sales and 29 percent of all commodities marketed by farmers, they must increasingly compete with firms much larger in size and that are better capitalized.

In addition, the businesses that farmer cooperatives buy from and sell to continue to grow in size. The top 10 firms in the farm supply food supply and food processing retailing sectors, for example, have average total sales of approximately $25 billion, more than six times greater than the average in the top 10 farmer-owned cooperatives.

Most significantly, no individual farmer cooperative has sufficient sales in any of these aggregate industry segments to be among the top 10 firms in the United States.

As was pointed out earlier in the chart, the farmer's share of consumer food dollars has now declined to where it just represents 20 cents, its lowest level ever. Reversing this decline would substantially improve the farmer's economic well-being and possibly reduce the impact of the budget on LDPs and other forms of direct payments to farmers.

If we could increase the share of the consumer dollar by just 1 cent from 20 to 21 cents, we would generate an additional $6 billion of income. The challenge, of course, is how do we, given the current business environment and ongoing trends, achieve this?

My view, the best way is to maintain and strengthen the ability of farmers to join together in cooperative self-help efforts. To be successful, however, we must make sure that we, as farmers, in our cooperative businesses are strategically positioned to be able to compete in what clearly is a rapidly changing global marketplace.

As was mentioned, our competitors and customers have grown in size, and we must challenge ourselves to be able to exist to survive and to this rife using similar strategies.

For this reason, I, as a farmer, am very concerned over various proposals to address the issue of ag concentration, however well intended they may be. That would make it more costly and difficult for farmers and our cooperatives to strategically position ourselves to compete in a changing global economy.

The practical effect may very well be to simply lock farmers such as myself and our cooperatives into a permanent disadvantage relative to our competitors.

And in business, if you don't meet the competition, you won't be in business very long.

There are, however, a number of actions that Congress and the Administration can and should take, based upon the recommendations of a special task force ag concentration established by the National Council Farmer Cooperatives.

These include maintaining and strengthen the ability of farmers to join together in cooperative self-help efforts, making sure our existing antitrust laws are fully enforced. That's been addressed today.

Maintaining the position of special counsel for agriculture within the U.S. Department of Justice along with needed funding. Support continuation of the existing memorandum of understanding involving USDA and Justice along with Federal Trade Commission to encourage cooperation on antitrust issues involving agriculture, and conducting a review of the Packer and Stockyards Act of 1921, as

well as the programs and responsibilities of USDA's grain inspection packer and stockyards administration to determine what additional authorities may be needed, if any.

Most important, I believe it is the need for public policies and programs to help maintain and strengthen the ability of farmers to join together in cooperative self-help efforts. I served as a cochairman of a task force with national counsel, and we identified several areas where we think some minimal changes in government policy would help farmers to help themselves.

By providing farmers and their cooperatives with improved access to capital to help gain ownership in value-added activities beyond the farm gate to invest in new equipment to modernize and expand and meet costly environmental and other regulatory requirements, additional capital is needed. Without access to capital, which is our greatest challenge, we will not succeed.

We can do this by increasing USDA's business and loan guarantee program for farmer cooperatives up to $10 million, and making it more consistent with similar programs for other cooperatives, such as rural electrics.

Clarifying existing authority for guaranteed loan programs for farmers to purchase stock in new value-added businesses to include both new and existing farmer-owned cooperatives, providing tax incentives to help attract capital, and encourage investment of farmer-owned cooperatives.

Enactment of the cooperative tax provisions included in Senate bill 312, as introduced by Senators Grassley, Baucus, and among others. Establishment of an equity capital fund as proposed previously by Senators Harkin and Craig to help farmers attract capital and investment.

In addition, a task force strongly recommended USDA and other Federal programs aimed at encouraging self-help by farmers be revitalized and given higher priority.

This would include establishing a separate USDA agency totally dedicated and focused on encouraging cooperative self-help, include research, technical, and education.

Six million, the new agency would be called the Farm Cooperative Business Service, and $6 million for the new agency to be called the Farm Cooperative Business Service, and $6 million for research, education, and technical assistance grant.

We also recommend that funding for value-added technical assistance grants authorized under the Ag Risk Protection Act of 2000 be increased from $15 to $25 million annually to enhance the ability of farmers to become more involved in value-added activities beyond the farm gate.

Together we believe these recommendations will provide farmers with greater opportunity to improve their income from marketplace to cooperative self-help efforts and promote competition.

PREPARED STATEMENT

Mr. Chairman, it has been said that a man with a full stomach has many problems, while a starving man has only one. So does it with our nation. Isn't it fantastic, thanks to the American farmer and American agribusiness, that we have a multitude of problems for you to deal with. I close my testimony. Thank you.

[The statement follows:]

PREPARED STATEMENT OF DAN KELLEY

Thank you, Mr. Chairman. My name is Dan Kelley and I am a producer from Normal, Illinois, where I am actively engaged in a farming partnership with my two brothers. Together, we operate a 2,080 acre diversified grain farm. I also serve as chairman of the board and president of GROWMARK, a federated regional farmer-owned farm supply and grain cooperative headquartered in Bloomington, Illinois.

Mr. Chairman, I want to commend you for this hearing. I also want to express appreciation to you and the Congress for the actions taken to help meet the near term challenges facing farmers. It appears that similar economic assistance will again be needed this year. At the same time, I am hopeful that we can begin to look at a more long term strategy to help farmers compete more effectively in a rapidly changing global economy and to generate more of their income from the marketplace.

As a federated regional cooperative, GROWMARK is owned and controlled by some 250,000 independent family farmers and their approximately 320 local cooperatives with total sales of nearly $1.4 billion. The majority of our members are in Illinois, Iowa and Wisconsin, but we are also experiencing growing membership in Indiana, Michigan and Ohio. The farmer owners that make up GROWMARK range in size from part-time "hobby farm" operators to full-time, family-owned, commercial operations with the average farm size being approximately 300 acres.

The mission of GROWMARK is to improve the long-term profitability of its farmer owners. Farmers joined together to form what is now GROWMARK to help ensure a dependable supply of critically needed farm-related inputs and enhanced opportunities to market their grain on a competitive basis. That purpose still exists today. As an independent family farmer, I can not stress just how important that continues to be, especially in today's business environment. Like all farmer cooperatives, GROWMARK has a unique accountability and focus because of the fact that it is farmer owned and farmer controlled.

Through its system of 320 local cooperatives, GROWMARK provides crop and livestock production inputs, petroleum products, consumer goods and grain marketing services to its farmer owners on a cost-effective and competitive basis. It also provides manufacturing, processing, quality control, product procurement and a range of other services to its local cooperatives for the benefit of their farmer owners.

As a cooperative, earnings from these activities are returned to GROWMARK's member owners on a patronage basis. Over the last 5 years, GROWMARK has returned more than $140 million in additional income to its members as a result of such "value-added" activities. This is significant given the business environment of the past 5 years.

Farmers today continue to operate in a very challenging business environment. Farm income continues to be highly variable due to the inherent risks involving production agriculture and the volatile nature of commodity markets. Commodity prices remain depressed. Production costs continue to increase. The global marketplace continues to be characterized by subsidized foreign competition and artificial trade barriers.

Globalization continues to drive changes throughout every sector of the economy. This has led to increasing consolidation at every level as businesses attempt to gain the size, scale and efficiencies needed to remain viable and competitive long term. This is underscored by recent mergers in the energy, chemical, insurance, banking, financial services, manufacturing, and transportation industries, as well as in agriculture, especially in the food processing and retailing sectors.

The National Council of Farmer Cooperatives (NCFC), a national trade association representing America's farmer owned cooperatives of which GROWMARK is a member, recently did an analysis of the relative position of farmer cooperatives in the food and agriculture system. Among the highlights, it found that—

While farmer cooperatives continue to play a significant role in the farm economy, accounting for 28 percent of all farm supply sales and 29 percent of all commodities marketed by farmers, they must increasingly compete with firms much larger in size and better capitalized.

In addition, the businesses that farmer cooperatives buy from or sell to continue to grow in size and market share.

The Top 10 firms in the farm supply, food processing and food retailing sectors, for example, have average total sales of approximately $25 billion—more than six times greater than the average for the Top 10 farmer owned cooperatives ($4 billion).

The Top 10 firms in the farm supply, food processing and food retailing sectors have increased their market share above 40 percent in each sector.

Most significantly, no individual farmer cooperative has sufficient sales in any of these aggregate industry segments to be among the Top 10 firms.

The farmer's share of the consumer food dollar has now declined to where it now represents just 20 cents—its lowest level ever. Reversing this decline would substantially improve the farmer's economic well being. For example, increasing the farmer's share of the consumer food dollar by just one cent to 21 cents would generate an additional $6 billion in income. The challenge of course is how, given the current business environment and ongoing trends.

In my view, the best way to help achieve this is to maintain and strengthen the ability of farmers to join together in cooperative self-help efforts. To be successful, however, we have to make sure we as farmers and our cooperative businesses are strategically positioned to be able to compete in what clearly is a rapidly changing global marketplace.

As our major competitors and customers have grown or consolidated to gain the size and scale needed to compete on a global basis, we have had to look at similar strategies. These have involved merging with other farmer cooperatives as well as entering into joint ventures and strategic alliances—to help reduce costs, be more competitive, and better meet customer demands in an effort to ensure that farmers like me continue to have access to competitively priced products as well as more competitive markets, and the opportunity to capture a greater share of the earnings related to such activities.

For this reason, as a farmer, I am very concerned over various proposals to address the issues of agriculture concentration, however well intended, that would make it more costly and difficult for farmers and their cooperatives to strategically position themselves to compete in a changing global economy. The practical effect would be simply to lock farmers and their cooperatives into a permanent disadvantage relative to their competitors. And, in business if you don't meet the competition, you won't be in business very long.

Again, it is important to emphasize that farmer cooperatives are farmer owned and farmer controlled. They operate on a democratic basis. When it comes to mergers and consolidations, not only must the board of directors, which is elected by the farmer owners from among themselves, approve the decision, but in most cases so must a majority of the cooperative's members. Many states (including Iowa, Minnesota, North and South Dakota, and Wisconsin) even require a two-thirds majority vote of a cooperative's members before a merger can be approved. For this reason, any proposal that would limit or restrict the ability of farmers like myself to determine what is in our mutual best interest, make it more costly, or make it more difficult to make timely business decisions should be opposed.

There are, however, a number of actions that Congress and the Administration can and should take based upon the recommendations of a special task force on agriculture concentration established by the National Council of Farmer Cooperatives. These include:

—Maintaining and strengthening the ability of farmers to join together in cooperative self-help efforts.

—Making sure existing antitrust laws are fully enforced. Currently, two Federal agencies—the U.S. Department of Justice (DOJ) and Federal Trade Commission (FTC)—and the state Attorneys General have enforcement power over agricultural mergers and acquisitions. The U.S. Department of Agriculture also plays a role and is consulted by DOJ and FTC under existing protocol.

—Maintaining the position of the Special Counsel for Agriculture within the U.S. Department of Justice, along with needed funding, to provide continued review and oversight with regard to agriculture antitrust issues.

—Supporting continuation of the existing memorandum of understanding (MOU) involving the U.S. Departments of Agriculture and Justice, along with the Federal Trade Commission, to encourage cooperation on antitrust issues involving agriculture.

—Conducting a review of the Packers and Stockyards Act of 1921, as well as the programs and responsibilities of USDA's Grain Inspection, Packers and Stockyards Administration (GIPSA) to determine what additional authorities may be needed, if any.

Most important, I believe, is the need to maintain and strengthen the ability of farmers to join together in cooperative self-help efforts. Such action—on a sustained basis—would help promote competition and maintain the independence of the family farmer. It would also provide farmers a greater opportunity to generate more of their income from the marketplace, capitalize on potential market opportunities,

better manage their risk, and compete more effectively in a rapidly changing global economy.

Again, it can not be overly emphasized, farmer cooperatives are farmer owned and controlled. They exist for the mutual benefit of their farmer members. There are nearly 3,500 local and regional farmer owned cooperatives across the U.S. whose member owners include a majority of the nation's nearly 2 million individual farmers. With nearly 300,000 full time and seasonal employees, they also provide a significant source of employment in many rural communities.

Joining together in cooperative self-help efforts provides farmers with the advantages of economies of scale and bargaining power, and the opportunity to participate in value-added activities beyond the farm gate. Earnings derived from related business activities are returned to the cooperative's farmer owners on a patronage basis.

A separate NCFC task force, on which I serve as co-chairman, has identified a number of actions that would help encourage and promote such cooperative self-help efforts. These include:

—Providing farmers and their cooperatives with improved access to capital to help gain ownership in value-added activities beyond the farm gate, to invest in new equipment, to modernize and expand, and meet costly environmental and other regulatory requirements. Without question, access to capital is one of the greatest challenges facing farmer cooperatives. To help meet this challenge, the task force recommended several options, including:

—Increasing USDA's Business and Industry Loan Guarantee Program for farmer cooperatives up to $10 billion and making it more consistent with similar programs for other types of cooperatives (such as rural electric cooperatives);

—Clarifying existing authority providing guaranteed loans to farmers for the purchase of stock in a new, value-added business, to include both new and existing farmer owned cooperative businesses for the same purpose;

—Providing tax incentives to help attract capital and encourage investment in farmer owned cooperative businesses;

—Enactment of the cooperative tax provisions included in S. 312 as introduced by Senators Grassley and Baucus, among others. Such legislation includes modification of the dividend allocation rule, which results in a triple tax on cooperative dividends on preferred stock, unfairly reduces the amount of patronage earnings that a cooperative may distribute to its members, and limits its use as a means of raising equity capital; and

Establishment of an equity capital fund such as that proposed previously by Senators Harkin and Craig, among others, that would help further provide farmer owned cooperatives and related businesses with improved access to capital.

In addition, the task force strongly recommended that existing Federal programs aimed at encouraging cooperative self-help efforts by farmers should be revitalized and given a high priority. To help achieve this, it was strongly recommended that Congress approve the establishment of a separate agency within USDA to be called the Farmer Cooperative Business Service and provide not less than $6 million annually for the purpose of carrying out and administering related research, education and technical assistance programs.

It also recommended that an additional $6 million be provided for cooperative research, education and technical assistance grants to be carried out through public-private partnerships involving associations, cooperatives, land grant colleges and universities, to further assist farmers, including limited resource farmers, in making the most effective use of the cooperative business model to improve their economic well being.

Finally, the task force recommended that funding for Value-Added Technical Assistance Grants authorized under the Agricultural Risk Protection Act of 2000 be increased from $15 million to $25 million annually to further enhance the ability of farmers to become more involved in value added activities beyond the farm gate.

Together, we believe these recommendations will provide farmers with a greater opportunity to improve their income from the marketplace, manage their risk, capitalize on potential market opportunities, compete more effectively in a rapidly changing global economy, and enhance their economic well being and profitability long term.

Mr. Chairman, this concludes my testimony. Again, I want to thank you for allowing me as an independent farmer to appear before you to discuss this important issue. I will be happy to answer any questions you or members of the Subcommittee may have.

Senator COCHRAN. Thank you, Mr. Kelley, for your interesting and provocative statement.

The Honorable Tom Miller is Attorney General of the State of Iowa. We'll hear from you now. Welcome.

STATEMENT OF TOM MILLER, ATTORNEY GENERAL, STATE OF IOWA

Mr. MILLER. Thank you very much, and I'll be brief, so brief I'll make one point, and then give an example to support the point.

The point I want to make, it's in my testimony, but I think it's very important, and that is that these issues that we're dealing with, concentration-related issues, antitrust and antitrust enforcement plays an important role in dealing with them, but far from an exclusive role. That what we need here is a comprehensive set of public policy principles and programs to deal with the issue.

And the example I give is this in contracting. In Iowa, we're probably seeing as much contracting as any State because contracting is moving forward in pork, probably more than in other parts of agriculture, and Iowa has about 25 percent of the PGGs in this country.

The concern is that we not let farmers become, because of imbalance in negotiating power, virtual serfs on their land. Like any situation, there are extreme positions to be avoided. We do not take the position that these contracts should be outlawed or prohibited in their entirety. They can be an important economic form.

Nor do we think that there should be no regulation at all so that we spiral into this sort of potential serfdom situation.

So what we did as attorney generals, as we often do, we work together. Sixteen States formed what we thought and believe are model producer protection legislation. Incidentally, Senator Dorgan, then Attorney General Heidi Heicamp, were cochair of that group last year when we worked on it among the 16 States, and we've sent you an outline of that legislation. It has to do with a ban on confidentiality, that it be transparent.

Now, the farmer makes the choice on whether it's disclosed or not. It's not automatically disclosed to everyone. The farmer or the contractor alone makes that call that certain unfair practices are dealt with in terms of retaliation for forming any kind of group activity, whistle blower, et cetera. Disclosure of risk is required.

There's a producer lien too that the farmer has the first lien on the animals. And there's restrictions on unfair cutting off the contracts, given the capital investments that the farmers have made.

We think these are realistic, fair provisions that give the farmer, who otherwise is in a very unequal negotiating position, some realistic ability to negotiate a fair contract that ultimately is in his interest, society's, and I would argue the contract owner's as well.

Senator Harkin, Senator Daschle, and others have introduced this legislation at the national level at the Senate, of course. We urge your consideration of that.

There are two real important parts of that legislation. One allows voluntary producer associations so that farmers can get together and negotiate or work with the contract owners on some group basis and requires good faith bargaining.

The other is a provision that allows the States to experiment and doesn't preempt the States. This, I think, is an important area for the laboratories of democracy in the States to work.

PREPARED STATEMENT

So I would ask you to take the middle ground here, not to stop these contracts but not to allow them to be totally one sided either, but to put some form of law in there that the farmer is given some meaningful position, some meaningful bargaining position so that this industry can flourish rather than having a situation where there are serfs on the land. Thank you both, Senators.

[The statement follows:]

PREPARED STATEMENT OF TOM MILLER

I want to thank the committee for this opportunity to testify on an issue of great concern to agricultural producers and consumers in my home state of Iowa and across the country—concentration in agriculture.

I, like many other state attorneys general, have become concerned about the rapid trend toward consolidation in agriculture at both horizontal and vertical levels. Through mergers, acquisitions, alliances, and other arrangements, fewer and fewer firms control the production, processing, preparation, and retailing of agricultural commodities and food. My worry is that this conglomeration of economic power may lead to anti-competitive practices and adversely affect the prices paid to farmers for commodities and the prices paid by consumers for food.

ANTITRUST ROLE OF STATE ATTORNEYS GENERAL IN AGRICULTURE

State attorneys general play a significant role in fostering full and free competition in the United States economy through the enforcement of Federal and State antitrust laws. We work in a multistate process to investigate and prosecute alleged anti-competitive activities in all sectors of the economy, including agriculture. We collaborate closely on these issues with the United States Department of Justice (USDOJ), the Federal Trade Commission, and the Packers and Stockyards Administration of the United States Department of Agriculture (USDA).

Examples of agricultural antitrust matters in which the states have been involved include a multimillion dollar settlement with major farm chemical manufacturers for alleged retail price maintenance, the Cargill/Continental merger, Smithfield Foods' acquisition of Murphy Family Farms, the Case/New Holland merger, and Tyson Foods' aborted acquisition of IBP. State attorneys general will continue to be vigilant in investigating allegations of anti-competitive behavior in agriculture and will vigorously enforce antitrust laws where appropriate. We particularly want to cooperate and share information with USDOJ and USDA.

However, in dealing with agricultural concentration and related issues, antitrust law is only one part of a possible solution to the problems farmers face today. For the antitrust law is a limited law as enacted and interpreted during the last century. Furthermore, the Federal courts in the last two decades have been restrictive in their interpretations of the antitrust law. The antitrust enforcers, including state attorney generals, must aggressively bring cases that fit within the antitrust law or arguably are within the prohibitions of the acts. But that will not solve all the problems that brought us here today. Antitrust is only part of the public policy approach to these issues.

OTHER ACTIVITIES OF STATE ATTORNEYS GENERAL

In addition to antitrust enforcement, state attorneys general have undertaken several other types of activities which we believe will help producers and others deal with the impacts of concentration in agriculture.

Agricultural Contracting

The use of production contracts and marketing contracts by firms with ever-growing market shares has dramatically increased vertical integration in American agriculture. Dr. Neil Harl, the noted agricultural economist and attorney from Iowa State University, has called this the "rising tide in contract agriculture."

There are important reasons why contractors (most often processors) and farmers utilize, and can benefit from, contracts. Indeed, some argue that contracting may greatly increase economic efficiency in agriculture. However, contracting poses serious risks for producers and, ultimately, for consumers. This is particularly true in some agricultural sectors where there is a high level of horizontal concentration combined with vertical linkages through contracts. In this situation, producers are,

as Dr. Harl puts it, "contracting with near monopolists." He calls this a "deadly combination."

Risks of Contracting

In general, contracting can pose several risks for producers, including the following:

Disparity in Bargaining Power

There is greater and greater disparity between processors and farmers with respect to market information and bargaining power. Large companies often offer contracts to producers on a "take it or leave it" basis. The contractual risks to producers are buried in pages of legalese and producers are stuck with unfair contract terms. In the poultry industry, which has been vertically integrated for decades through the extensive use of contracts, we hear repeated allegations of unfair treatment of producers.

Unfair Shifting of Risk

Contracting can result in the unfair shifting of economic risks to farmers. This is common in production contracts that require producers to make substantial capital investments. For example, in the poultry industry, some producers are contractually required to make long term capital investments in buildings and equipment, but are only offered a contract that covers one flock of birds.

Loss of Market Transparency

The first lesson of "Economics 101" is that economic efficiency can only be attained in a free market if market participants have adequate information to make economic decisions. The importance of market transparency and price discovery is so fundamental that it is academic dogma.

Traditionally, a hallmark of American agriculture was the free flow of market information available through auctions, terminals, and futures trading. Sadly, that situation has changed dramatically. Today, agricultural production and marketing contracts routinely contain strict confidentiality clauses. (As discussed below, this is not true in Iowa where confidentiality clauses are prohibited.) Some confidentiality clauses are so restrictive that farmers are reluctant to consult with their lawyers and financial advisors. As a result, most agricultural contracting is conducted in virtual secrecy, which severely limits the ability of farmers to compare contracts and negotiate the best, or even a fair, deal.

State Legislation—the "Producer Protection Act."

States have an opportunity and indeed a responsibility to consider reasonable oversight of agricultural contracting that will lessen the risks of contracting and promote meaningful competition in agriculture.

Our work in production contracting began with educational efforts for producers. In 1995, I formed the "Attorney General's Task Force on Production Contracts" that developed grain and livestock production contract checklists to help farmers negotiate production contracts. The checklists have been widely distributed throughout the country via the Internet.

Producer education is important. However, as the number of complaints about contracting filed with my Farm Division increased, I became convinced legislation was necessary. Last year, I led a group of state attorneys general in an effort to develop model state legislation on contracting. The goal was to draft provisions that would provide needed protections for farmers without overly burdening processors. The product was model state legislation entitled the "Producer Protection Act." The legislation was endorsed in principle by the Attorneys General of Colorado, Indiana, Kentucky, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, North Dakota, Oklahoma, Vermont, West Virginia, Wisconsin, and Wyoming.

In brief, the Act has several noteworthy provisions:

Bans on Confidentiality

Based on an Iowa statute passed in 1999, the Act prohibits the inclusion of confidentiality provisions in agricultural production and marketing contracts. This prohibition would allow producers to freely share their contracts with lawyers, bankers, other producers, and government officials.

Utilizing the protections of Iowa's law, my Farm Division has taken about 70 different types of contracts provided by producers and put them on our website (with producers' names deleted). This website (www.iowaattorneygeneral.org) is one of the few places in the nation where producers can obtain information needed to compare price and other terms and conditions of contracts. We believe this information will enable farmers to negotiate better deals.

Unfair Practices

The model Act makes it an unfair practice for processors to retaliate or discriminate against producers who exercise certain rights, including the right to join producer organizations, to freely contract with others, and to be a "whisteblower." In Iowa, we have received an increasing number of reports that contractors have made threats to retaliate if producers file complaints about contractual problems with our Farm Division or exercise statutory rights (e.g., filing a contract producer lien). The threats have included threats to provide substandard animals and threats to terminate or not renew contracts.

Disclosure of Risks

The model Act requires contracts to include a cover page which must contain a disclosure of material risks written in plain language. This is based on a Minnesota law passed in 2000 that has proven to be quite helpful to producers.

Right to Review

Similar to protections found in consumer law (e.g., door-to-door sales rules), the model Act provides contract producers with a three-day right to review production contracts.

Contract Producer Lien

Based on a 1999 Iowa statute, the model Act provides producers with a first priority lien for payments due under a production contract. This alleviates one of the real risks faced by producers in production contracting—getting paid.

Capital Investments

The model Act makes it harder for processors to terminate production contracts capriciously or as a form of retribution if farmers have already made sizable capital investments pursuant to requirements in the contracts.

Since the Producer Protection Act was announced in September of 2000, state attorneys general have worked with various farm groups, agribusinesses, governors, state agriculture commissioners, and legislators to revise and improve the legislation as needed in their respective states. Eighteen state legislatures considered various versions of the Act. No state has passed all parts of the Act (although, as mentioned, segments of it are already law in Iowa and other states). We will continue to cooperate with interested parties and decision makers in the coming years to see effective and reasonable state legislation enacted.

Federal Legislation on Contracting

Federal legislation has been introduced that closely resembles the states' Producer Protection Act. I strongly support the concept of enacting Federal protections which mirror the states' proposals. One of the goals of the model state legislation was to encourage a similar state framework for the regulation of contracting. The idea was to avoid a patchwork of divergent state laws and the regulatory burden it would place on agribusinesses. Obviously, Federal legislation would accomplish this goal.

However, if Federal legislation is enacted, it is crucial that states are not preempted in their ability to grant producers additional protections based on the specific needs existing in a state.

AGRICULTURAL FAIR PRACTICES AND PRODUCER ASSOCIATIONS

There is no question that farmers and ranchers now more than ever need to join together to bargain for better contractual terms with large agribusinesses. Many believe that the lopsided disparity in bargaining power between producers and processors can only be corrected if producers forge alliances. As Dr. Neil Harl states, "Historically, farmers have been unwilling to accept such a disciplined approach to achieving bargaining power. However, the time may be near when that will be the only practical alternative to vulnerability and serfdom."

States are currently limited in their ability to enact legislation in the area of collective bargaining for agricultural producers due to preemption language in the Agricultural Fair Practices Act of 1967 (AFPA). Fortunately, Federal legislation has been introduced in this area which contains two important components:

Producers' Ability to Bargain Strengthened

The proposed Federal legislation establishes a process by which voluntary producer associations can receive accreditation from USDA. In turn, these accredited associations are authorized to bargain with large processors, contractors, and cooperatives (defined as "designated handlers" in the legislation). Mutual obligations of good faith bargaining are imposed on both the accredited associations and the designated handlers.

Additionally, the Federal legislation strengthens the ability of producers to organize associations without fearing coercion, intimidation, or discrimination by large agribusinesses as a result.

State Laws Not Preempted

Significantly, the Federal legislation makes clear that state laws dealing with producer bargaining are not invalidated by Federal law (i.e., the AFPA).

I would strongly encourage the enactment of this Federal legislation. Farmers across the country would then have the tools needed to band together and negotiate agreements which, hopefully, would give them their fair share of the profits available in production agriculture.

In summary, state attorneys general will continue to aggressively enforce antitrust laws, but will also press for state and Federal legislation which we believe will be more effective in dealing with the negative impacts of consolidation in agriculture.

Again, I thank the committee for the opportunity to discuss this serious problem.

Senator COCHRAN. Thank you, Mr. Miller.

Mr. David Reis, President-Elect Illinois Pork Producers. Welcome.

STATEMENT OF DAVID REIS, PRESIDENT-ELECT, ILLINOIS PORK PRODUCERS

Mr. REIS. Thank you, Chairman Cochran, and members of the committee. As you said, my name is David Reis. I'm a pork producer in Illinois, St. Real, Illinois. I'm currently serving as President-Elect of Illinois Pork Producers Association and also as a volunteer consultant to and a member of the American Premium Foods Cooperative.

It is truly an honor to be here before this subcommittee on behalf of the over 240 members of the independent pork producers of our co-op to set a different angle on what we're trying to do to deal with the changing agricultural industry.

We've heard a lot of testimony today about the fact that agriculture is going through a period of change and transition and consolidation. The result is the traditional family farm is giving way to a system of contracted and integrated corporate operations.

And in some of the producer groups and producers themselves have resorted to spending a lot of their time and resources on trying to figure out how they can stop this trend, whether it's price control measures or moratoriums on mergers and acquisitions or whatever it might be.

But a couple of years ago we at American Premium Foods took another approach, and we wanted to be proactive and engage in activities that would allow us to not only to control our own destinies but also to create more jobs in the communities in which we live and offer economic stimulus to that area.

We wanted to provide or establish a correlation between the prices that consumers are paying for their products and what farmers are receiving for their commodities.

American Premium Foods was organized in late 1999 after almost a year of business plan development and membership recruitment by its founding leadership. It's comprised of independent pork producers from throughout Illinois. We plan to construct a pork packing and fresh processing facility that is capable of handling 2,800 head per day.

The plant will be one of the most automated and sanitary in the United States. In our facility, even with the equipment and strin-

gent homework that we're going into, it will even meet the tough European Union standards so we'll be able to export our meat to other countries. No other plant in the United States will have that.

We'll market our meat under the newly formed Meadow Brook Farms label in which American Premium Foods owns a 51 percent majority of. The farmers also own the brand name label that we're going to establish after that.

Each carcass going through this plant will be individually tracked. The producer members will be paid for, the wholesale value of the primal cuts from their hogs. Profits from additional processing as they come in will be paid out according to the producer's percentage ownership in the plant.

Our $30 million-dollar facility will employ 210 people and will have an annual payroll of approximately $6 million. Because of its smaller size, the plant is designed to be an environmentally friendly asset to the community in which we choose to put it.

You hear so many stories about these large plants moving into town, and they're 10,000 12,000, 16,000 head a day, and they run into opposition. We feel that the site will be friendly to that community in which we choose.

Our project, as smooth as it may sound, hasn't been without its share of problems and attack from critics and non-supporters. Because this venture of this size is the first one in the country, we don't have a business model to follow.

It was deemed high risk start up from banks and not only the banks that are going to be loaning the money to the cooperative, but the banks would be loaning the money to the individual producers that are buying their shares and providing their part of the equity.

We are advised to be aware of snake oil salesmen, that this is a concept that couldn't work in getting back to the equity part of the producer's equity was lost in the low hog prices in 1998. Here they were, they lost their equity, we knew we had a problem. Now they're wanting to invest in something that might help them get out of that.

So all of those things, as you can tell, is real easy for the critics to sit back and say this can't be done. But I'm proud of the group. It's held its course, and it's continued to believe that what we're doing is worth fighting for. Because truly what's at stake is the existence of the independent pork producer, the ones that are left.

We've been, as I said, working on this project for 2 years now. But each day that passes, the consolidation that everyone has talked here about today continues. We need to move projects like this forward.

Just a few weeks ago it was announced that Seaport Corporation has scrapped its plans to build a new processing plant in Kansas. This gives proof that and confirms that most of the growth incurred by these large packing plants is through acquisitions and mergers. They're not investing in new facilities.

And the talk of the news now is that high fuel costs are a result of an industry that hasn't continued to reinvest in itself. There is some correlation there with that industry.

So what can the Senate Appropriations Committee do to help? We need common sense solutions and assistance if more projects

such as ours are going to successfully move through the critical period of planning and start up. Whether it's beef or pork packing plants, soybean crushing plants, ethanol production, aquaculture, or many other value-added consents are being discussed. Oftentimes the difference between success and failure is the amount of time spent doing the preliminary work. And this all takes a lot of time and a lot of money.

These ventures need assistance in hiring the best firms to do the feasibility studies, the business plan development, the market plan development. We know how to raise pork in a pork industry. We know how to do it better than anyone else in the world. We need a little boost here in terms of not only assistance in paying for consultation but maybe centers that could help us do with that research to help us in a broader sense with ventures as large as this. So as we spread out, we need a little help getting there.

So that we offer these suggestions, allow and encourage all agencies and their employees associated with value-added co-op development to instill a positive attitude and to look for solutions, not obstacles, when consulting projects like ours.

Right now there seems to be incentives only for writing good loans and not all loans are good. So let's take a look at this operation and what can we do to help you folks.

Dramatically streamline the grant and loan application process and fund these programs at a higher level. We talked about the Grassley value-added grant application. That's one thing. I think the rules there can be streamlined a little bit. And with the USDA-backed loans, it shouldn't take 15 to 16 months to get through a process. I don't know if the States vary in their level that they can go up to, but in Illinois it's $10 million.

You go through several months of going through the process and they say, well, we need to refer you to the USDA in Washington. So then you go through all of this process again and this all takes time.

I really didn't say about the time, but all the time we're spending on this we still have to run our farms. We're short of labor, we're short of cash to pay the labor. Our wives work in town. And being gone 2 or 3 days a week for 2 years, it starts taking a toll on us. I wanted to reemphasize it on the time.

Another option is introduce and pass legislation that offers tax incentives to members who invest in new generation co-ops. And, lastly, an example that was talked about, several States have value-added bills and rules that they are currently working with. Maybe a block grant to those States that maybe matches their funds if they put in $5 million and another 5 million would come from the Federal Government.

In closing, Mr. Chairman, members of the committee, the producers in our group have pretty much laid their operations on the line. They've invested a lot of sweat equity and time and money and are going to be investing a lot of money when we make the capital call on this operation. They feel that the future of independent pork producers relies on this, the key ingredient in our rural economy.

And we hope that through the testimony from all of these people that we can work together to find common sense ways to help oper-

ations such as or projects such as ours get up and get going. So I want to thank you for your invitation and be happy to answer any questions.

Senator COCHRAN. Thank you, Mr. Reis. We appreciate your contribution to this hearing and all of the members of this panel. We're grateful to you for the time you took to prepare statements and think about the subject we had under review today. And to add to our understanding of some of the challenges that we face. And also to open our minds to new ideas and suggestions for ways to improve the opportunities for farmers and production agriculture to operate their enterprises profitably.

And some new suggestions about how to get out of the problem of concentration and ensure that we do have the opportunity that results in fair chances to sell at fair prices the products that are produced.

Mr. MILLER. Senator, we appreciate you sitting through 2½ hours so we could all have our say here. Thank you.

Senator COCHRAN. I am interested in the suggestions. I thought Mr. Butler's comments about the arbitration clauses were provoking. We need to be sure that there is a fair opportunity to have disagreements dealt with. And we shouldn't prefer one side over the other in these arrangements.

And so we need to look at that again to see what we can do at the Federal level. Whether or not the State legislatures have more of a role to play in some of the local laws and practices as well.

But I'm hopeful that we will all benefit from this, and as we go through our appropriations bill this year and look at the requests we have from the different agencies at the Department of Agriculture for funding, we'll look at some of the suggestions we got today and consider them very seriously. I know you had some specific suggestions, and we appreciate that. Other witnesses did as well.

CONCLUSION OF HEARING

Senator COCHRAN. We appreciate your attendance, and the hearing is recessed.

[Whereupon, at 12:40 p.m., Thursday, May 17, the hearing was concluded and the subcommittee was recessed, to reconvene subject to the call of the Chair.]

Material Submitted Subsequent to Conclusion of Hearing

[CLERK'S NOTE.—The following statement was received by the subcommittee subsequent to the conclusion of the hearing. The statement will be inserted in the record at this point.]

[The statement follows:]

PREPARED STATEMENT OF THE AMERICAN COTTON SHIPPERS ASSOCIATION

The American Cotton Shippers Association is opposed to the enactment of the legislation that would impose on the cotton industry and its highly competitive marketing system the oversight of the Federal Government.

INTEREST OF ACSA

ACSA was founded in 1924 and is composed of primary buyers, mill service agents, merchants, shippers, and exporters of raw cotton who are members of four federated associations located in sixteen states throughout the cotton belt:

Atlantic Cotton Association (AL, FL, GA, NC, SC, & VA) Southern Cotton Association (AR, LA, MS, MO, & TN) Texas Cotton Association (OK & TX) Western Cotton Shippers Association (AZ, CA, & NM)

ACSA member firms handle over 80 percent of the U.S. cotton sold in domestic and export markets. In 2000–2001, domestic mills will consume 10.25 million bales and 6.75 million bales will be shipped to foreign mills. Because of their involvement in the sale and shipment of cotton, ACSA members are directly impacted by any action of the Congress that impedes their ability to purchase the product of America's cotton producers at competitive prices. Therefore, our interest is manifest in the proposal before the Subcommittee since the pricing and marketing of US cotton is a sound and effective example of a highly competitive deregulated system that functions in the best interests of our producer, domestic mill, and export customers.

Proposed Legislation Restricts Competitive Marketing of Cotton Legislation introduced in the 106th Congress, S. 2252, The Agriculture Competition Enhancement Act, and S. 2411, The Farmers and Ranchers Fair Competition Act of 2000 and pending legislation S. 20, Securing a Future for Independent Agriculture Act of 2001, in the 107th Congress would have an adverse impact on the marketing of cotton.

At the heart of each measure is a section which will result in USDA regulation of cotton purchases and sales by making it unlawful for any dealer, processor, commission merchant, or broker to make or give any undue or unreasonable preference or advantage to any particular person or locality or subject any particular person or locality to any undue or unreasonable disadvantage in connection with any transaction involving any agricultural commodity.

The concerns over market concentration in sectors of the livestock industry will have the effect of regulating cotton sales and threatens a marketing structure, which over the years has provided cotton producers with an active and competitive market for the sale of cotton.

This provision will preclude the offering of price premiums to areas of the cotton belt that produce high quality fiber with strong market demand and the establishment of discounts for poor fiber qualities in other areas. In instances of a short world supply of poorer quality fibers this could result in a premium for the lower qualities, given its world demand, over that of finer qualities produced in that or other regions of the United States. Would such market circumstances be subject to the review of USDA?

Further, this unnecessary and restrictive language precludes discounts for cotton produced and stored in areas where warehouse service is poor and delays are frequently encountered and prohibits the payment of premiums in areas where the warehouses provide timely or even immediate shipment.

This provision would also create havoc with forward contracts entered into with producers from the same region at different points in time at different fixed prices or prices determined by futures market prices. Those who contract at different times or fix the futures price in different months could be deemed to have "an unreasonable preference or advantage." The same is true for those who sell in the spot market at different points in time. All of these situations establish prices and the last thing our industry needs is a USDA bureau determining that marketing factors "subject any particular person or locality to any undue or unreasonable prejudice or disadvantage."

We also have concerns with the restrictions on the sale or acquisition of relatively small merchant businesses, warehouses, and cotton gins with annual net sales of more than $10 million, which is equivalent to handling approximately 25,000 bales of cotton.

INTERFERENCE WITH CONTRACTING PROCESS IS A GRIEVOUS & UNNECESSARY OVERREACHING BY FEDERAL GOVERNMENT

The premise of S. 20 in Subtitle C, Contract Fairness, Section 121 is that agricultural contracts are not entered into in good faith with respect to performance and enforcement and that producers are unsophisticated and unfamiliar with their contractual rights in a competitive marketplace. This erroneous premise ignores the Common Law contract rights of the parties to agricultural contracts, which are incorporated in the Uniform Commercial Code and continually updated by the National Conference of Commissioners on Uniform State Laws and the American Law Institute to reflect patterns of trade, customs and usages and court decisions. It ignores the educational programs of producer and trade organizations on the contracting process, and the transparent process of the cotton industry, which has utilized fully explained uniform contracts for over 25 years. Additionally, to subject contract provisions to the approval of the Secretary of Agriculture is a grievous and unnecessary overreaching of the independent rights of contracting parties, as is the right of parties for mutually desirable and agreeable reasons to maintain the confidential nature of their lawful contract terms and conditions. Further, establishing a Central Filing System for the purposes of perfecting liens was recently considered and rejected by the Congress in its recent review and updating of the Federal Warehouse Act. Most disturbing is the proposal to void the long established policy of the US Congress to foster the use of arbitration when contractual disputes cannot be amicably resolved. Arbitration is available to cotton, wheat, feed grain and oil seed producers throughout the United States and provides a fair, efficient, and inexpensive recourse to dispute resolution. To suggest otherwise would contravene the numerous favorable decisions of the state and Federal judiciary and repudiate a sound public policy and well established and accepted industry practice.

NO COMPELLING NEED & NO DEMAND FOR REGULATION OF COTTON INDUSTRY

This one-size-fits-all regulatory reaction to the transitional nature of the livestock production and processing sector and the current oversupplied US and world farm economies will do nothing more than worsen the situation. In our view there is no real or government fabricated substitute for competition.

The cotton marketing system is a proven success and a competitive model well suited for the US cotton industry. In no other sector of the farm economy is the factor of competition more prevalent than in the cotton industry. There is no justification for its regulation and the producer segment of our industry has not expressed a desire that cotton be subjected to the provisions of S. 20, S. 2252 or S. 2411. In fact the National Cotton Council of America has an express policies in opposition to such legislation. Therefore, we respectfully request that any consideration exempt cotton and the other price supported commodities from inclusion in the proposed legislation.

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