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GRAIN INSPECTION, PACKERS AND STOCKYARDS ADMINISTRATION OVERSIGHT

HEARING

BEFORE THE

COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY UNITED STATES SENATE

ONE HUNDRED SIXTH CONGRESS

SECOND SESSION

ON

GRAIN INSPECTION, PACKERS AND STOCKYARDS ADMINISTRATION OVERSIGHT

February 1, 2000

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PACKERS AND STOCKYARDS ADMINISTRATION

TUESDAY, FEBRUARY 1, 2000

U.S. SENATE,
COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY,
Washington, DC.

The Committee met, pursuant to notice, at 9:00 a.m., in room 328A, Russell Senate Office Building, Hon. Richard Lugar, (Chairman of the Committee), presiding.

Present or submitting a statement: Senators Lugar, Roberts, Fitzgerald, Grassley, Craig, Harkin, Leahy, Conrad, Baucus, Feingold, and Hagel.

STATEMENT OF HON. RICHARD G. LUGAR, A U.S. SENATOR FROM INDIANA, CHAIRMAN, COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY

The CHAIRMAN. This hearing of the Senate Agriculture Committee is called to order.

Let me point out that agriculture in the United States is experiencing a significant transformation. This evolution can be attributed to rapidly improving technologies, developments in biotechnology, changes in worldwide consumption, and concentration in production agriculture and agribusiness. These developments create opportunities but they also raise questions about concentration and antitrust. The developments also raise new challenges in the regulation of unfair and deceptive business practices and identifying the best policies to address these issues.

This Committee has examined the concentration issues in previous hearings. The competitive implications of consolidation and concentration in production agriculture and agribusiness are clearly numerous. Situations of monopoly or monopsony can result from the reduction in the number of market participants or an increase in the market share of the participants.

Unique among Federal statutes that are within the purview of the Department of Agriculture are the Packers and Stockyards Act, which provides the Secretary with the legal authority to take action against activities by packers in interstate commerce that have the effect of restraining commerce or creating a monopoly in commerce. The USDA has restructured the Grain Inspection, Packers and Stockyards Administration to strengthen enforcement of anticompetitive practices and to improve the Agency's ability to enforce the provisions of the Packers and Stockyards Act.

Today the Committee will examine the present structure and functions of the Grain Inspection, Packers and Stockyards Adminis-

tration. The marriage of two previously independent agencies occurred in 1994, intended to secure a production and competitive global marketplace for U.S. agricultural products.

I will welcome in a moment Mr. Michael Dunn, Under Secretary for Marketing and Regulatory Programs; Mr. James Baker, Administrator of the Grain Inspection, Packers and Stockyards Administration [GIPSA]. I have asked Mr. Baker to provide testimony addressing the challenges facing GIPSA and Under Secretary Dunn may offer additional comments to our hearing.

I thank Mr. Baker in advance for coming to my home State of Indiana in order to receive input from Hoosier farmers regarding concentration and consolidation. It is a major issue in our state. I also welcome Mr. David Shipman, Deputy Administrator of the Federal Grain Inspection Program, who is present to respond to questions the Committee may have regarding this program.

I am pleased that Dr. Philip Paarlberg and Dr. Kenneth Foster from Purdue University are with us today. They will review findings in their recent paper entitled "Structural Change and Market Performance in Agriculture: Critical Issues and Concerns about Concentration in the Pork Industry."

Today's third panel contains producer representatives who will provide commentary on the functions performed by the Packers and Stockyards Administration. And finally, the last panel consists of members from producer groups and the business community who will discuss the functions assigned to the Federal Grain Inspection Program.

Senator Hagel's statement will be made a part of the record.

It is my privilege, first of all, to welcome my distinguished colleague Senator Feingold of Wisconsin, who will offer testimony and then be on his way, unless he wishes to participate in the hearing further. Russ, it is good to have you this morning.

[The prepared statement of Senator Hagel can be found in the appendix on page 79.]

[The prepared statement of Senator Lugar can be found in the appendix on page 78.]

STATEMENT OF HON. RUSSELL FEINGOLD, A U.S. SENATOR FROM WISCONSIN

Senator FEINGOLD. Thank you very much, Mr. Chairman, for having the hearing and for letting me make some comments. As a former member of this Committee, it is a great opportunity to discuss something of tremendous importance to people in my state.

I am pleased to be here this morning to briefly discuss the effects of the increased consolidation and concentration rolling through America's agricultural industry, which is causing disruption for many farmers and actual ruin for others. I am particularly concerned about these changes to the structure of the U.S. agriculture industry because of the effect it is having on family farms.

Over the past 70-years, Mr. Chairman, we have certainly seen a transformation of America's agricultural sector. As U.S. farms have consolidated, their numbers have declined from there being nearly 7 million farms in the 1930s to about 2.2 million in 1998. Many farmers believe through bitter experience that consolidation in the agriculture industry has put the economic opportunity that many

others are experiencing in this country out of reach for some of America's small family farmers.

I want to be clear, because this is far too complex a subject to oversimplify, that I realize that consolidation of our agriculture industry is not the root of all of our farmers' problems. I am not blaming low commodity prices solely on the mergers in corporate America on the increased consolidation of our nation's farms. But surely these trends are a big part of the problem for a small farm.

As I travel to each of Wisconsin's 72 counties each year, I hear again and again that increased market concentration means less negotiating power for the men and women who actually produce our dairy products, our grain and our livestock. And sometimes, as I am sure you have experienced, Mr. Chairman and my colleague from Montana, I am sure you have heard these stories from proud, hard-working farmers who wonder if or fear that the loss of power that they are experiencing will mean that they will be the last generation in their family who will be able to farm.

Farmers understand all too well that increased concentration in the agriculture industry has led to inadequate market access for small and medium-sized farmers and has also resulted in price discrimination against small, independent producers.

I am pleased that you, Mr. Chairman, have agreed to hold this hearing on the subject of the Grain Inspection, Packers and Stockyards Administration. After all, the Packers and Stockyards Act is one of the strongest antitrust laws ever written in this country and certainly one of the most important to our nation's agricultural industry. Its goal is to protect livestock producers and meat consumers from the potential use by packers of a monopoly power to unduly lower the prices paid to producers and to raise prices for consumers.

As many of you know, this legislation was originally passed to break up the so-called Beef Trust, a group of five packing companies that controlled a large percentage of the beef and hog slaughter throughout the country. Ironically, the concentration levels in the beef packing industry at the time that the Packers and Stockyards Act was enacted are roughly the same as they are today. A 1916 Federal Trade Commission report found that the Big Five packers controlled 82.2-percent of the cattle slaughter. Today the top five beef packers control as much as 83-percent of the beef slaughter, and the same trend has occurred in the pork industry. According to the 1916 report, the top five packing firms controlled 61-percent of the hog slaughter; today the top four packers control 57-percent and the top seven firms control 75-percent of the hog slaughter.

This trend toward market concentration in these industries is alarming and it must be addressed with the same vigor that our predecessors in Congress brought to their effort to pass the Packers and Stockyards Act nearly a century ago.

I further urge GIPSA to fully enforce its authority through Section 202 and other means to protect our farmers against price discrimination in the grain and livestock markets. Unless we protect our independent producers against price discrimination, we will be left with only a few giant firms that get to call the shots and eco-

nomic devastation in many rural communities throughout the United States.

Independent producers, whether they are hog producers, cattlemen, dairy producers or soybean farmers, have a dwindling number of markets available to them and face significant price discrimination. Last year alone the GAO reported that during an 18-month period, slaughter capacity in the pork industry decreased by 9-percent. In my State of Wisconsin, many hog farmers have to ship their animals as far as Iowa or Illinois. Even in these states there are fewer and fewer slaughtering plants each year.

All indicators in the pork industry point to producers receiving an increasingly smaller share of the retail dollar. Last year, for example, when producer prices went down over 60-percent, USDA reported that consumers were only paying 3-percent less. While that money is going somewhere, it is certainly not going to the farmers.

Of particular concern in Wisconsin, Mr. Chairman, are the mergers of large dairy coops. In the last few years we have seen the mergers of Mid-America Dairymen, the Associated Milk Producers, Milk Marketing and the Western Dairymen Cooperative. These coops were the first, second, third and twelfth largest in the country and they all joined together to form the Dairy Farmers of America, now the largest coop in the country, and it handles over 26-percent of the country's milk. Land o'Lakes recently acquired Atlantic Dairy, then merged with Dairyman's Creamer. Last week Land o'Lakes bought Madison Dairy Produce, Inc., which turns about 15-percent of the Nation's butter.

However, the merger of these coops and their exemption from antitrust laws under the Capper-olstead Act of 1922 may only be a small part of the problem because we also have a tremendous number of mergers in the retail grocery industry. Over the past 2-years, Dean Foods has announced its acquisition of more than 11 smaller retailers. Based on USDA numbers, it seems that the bargaining power of large grocery chains represents a significant threat to our dairy farmers' profit margins. Retailers made 70 cents per gallon in 1992 when the store price was $2.78. So the grocery store was raking in 25.5-percent of the earnings in total per hundredweight.

These figures, Mr. Chairman, invite the question: are retail prices affected by these mergers? How else can one explain that 10-years ago, farmers were getting $1 more per hundredweight for their milk than they are now but retail prices were actually $1 less than today's prices.

Again I am not here to blame the low commodity prices solely on the coops and the retailers and mergers in corporate America. However, we in Congress must take a hard look at the antitrust laws to make sure that they effectively deal with the problems of concentration that we are now seeing.

Until the Senate passes comprehensive agricultural antitrust reform legislation, I will continue to push for the Agribusiness Merger Moratorium Act of 1999, which places strict limits on market concentration in the agricultural industry by preventing large agribusiness mergers.

This country, Mr. Chairman, is in grave danger of losing its independent producers—hog producers, cattlemen, dairy producers, soy-

bean farmers and others. We are in danger of losing a rich tradition, of losing the capacity to honor and reward generations of hard work and the love of the land.

Our nation's farmers are a key pillar of the economy, both rural and urban. In Wisconsin, the dairy industry alone generates around $10 billion for the state's economy.

I commend USDA for taking the initiative on small farms. I am also pleased that the Department of Justice has brought on board a senior enforcement attorney whose staff will deal solely with agricultural antitrust issues. However, our work is far from done because the level of market concentration in some key sectors is the same, as I said, as it was when Congress passed the Packers and Stockyards Act way back in 1921. We must enable all producers to have a fair shot in the marketplace and we must be mindful of the human consequences for our country if we fail to do that and do it soon.

I am grateful for all the time and for the opportunity to testify, Mr. Chairman.

The CHAIRMAN. Well, we are grateful for your testimony, your experience in this issue.

Senator Baucus, do you have a question for our witness?

STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM MONTANA

Senator BAUCUS. I would just like to commend Senator Feingold on his very thoughtful statement. He is finding in Wisconsin, as we all are in all parts of the country, that producers are in deep trouble. It is a serious problem, as you know, Mr. Chairman, and you outlined the key points, Senator, namely the concentration in the packing industry and the cattle and dairy coops, the mergers of retailers.

And it is true that,that is not the sole cause of the problems. There is no doubt about that. But it just kind of feels like, smells like, seems like it is still a part of the problem, and it is a key part of the problem. It is one that must be addressed.

And clearly we, as Americans, want to continue to have the most prosperous agriculture industry in the world but we want our producers to be part of it. And it is very important that we look at legislation like that suggested by Senator Feingold, Mr. Chairman, as well as other legislation that I am sure is going to be offered because we do not want unintended consequences, either. We have to be smart about this. But being smart, to me, means recognizing there is a serious problem and addressing it, and also addressing it in a way that does not throw the baby out with the bathwater or upset the applecart, not to mix metaphors here, but to do it in a smart way.

But it is going to take time. It is going to take a lot of work for us to try to figure out what legislation seems to make the most sense here and has the greatest positive effect for the greatest number of Americans.

But I very much compliment you, Senator, on your statement. You have touched on the problem, hit the nail on the head here and by the tone of your statement, you clearly want to do this fair-

ly and in a solid, responsible way, but it has to be done. Thank you very much.

Senator FEINGOLD. Thank you, Senator Baucus.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you very much for your testimony. I would just follow through on the distinguished senator from Montana's comments and I am certain he has read the back-up for this hearing, as well as the testimony that we are about to hear, and these issues are not necessarily of dazzling complexity but still the thought of doing something that does not have unintended consequences is a good point. There will be legislative suggestions today in some of the testimony and we welcome those, but it is an invitation for all members to be very observant of all of the by-play. There are counterthoughts for almost each of the suggestions we are going to have.

Unfortunately, Congressman Gilchrest, who had hoped to come to testify, will not be able to do so.

[The prepared statement of Congressman Gilchrest can be found in the appendix on page 76.]

Therefore we will move on to our first panel, which includes Mr. Michael Dunn, the Under Secretary for Marketing and Regulatory Programs at the United States Department of Agriculture; and Mr. James R. Baker, Administrator of the Grain Inspection, Packers and Stockyards Administration of the United States Department of Agriculture. They are accompanied by Mr. David Shipman, the Deputy Administrator of the Federal Grain Inspection Program.

Gentlemen, we are very pleased to have you here this morning. We appreciate the time you have given already in preparation of testimony, as well as your experience in the issues before us.

I would like to call first upon Mr. Baker for his testimony, who will be followed then by comments that Mr. Dunn may have, and Mr. Shipman is available for questions that may arise or other expert points that need to be made.

Mr. Baker, would you please proceed?

STATEMENT OF JAMES R. BAKER, ADMINISTRATOR, GRAIN INSPECTION, PACKERS AND STOCKYARDS ADMINISTRATION, U.S. DEPARTMENT OF AGRICULTURE, ACCOMPANIED BY DAVID SHIPMAN, DEPUTY ADMINISTRATOR, FEDERAL GRAIN INSPECTION PROGRAM

Mr. BAKER. Thank you, Mr. Chairman and members of the Committee. I am proud to come before you today and talk about the Grain Inspection, Packers and Stockyards programs. A complete written statement will be submitted for the record.

GIPSA was established under the authority of the Department of Agriculture Reorganization Act of 1994. We are probably the youngest agency in the Department of Agriculture. The agency's services and programs facilitate the marketing of livestock, poultry, meat, cereals, oilseeds and related agricultural products for the overall benefit of consumers of American agriculture. The agency carries on a tradition of service, integrity and professionalism and fairness that characterizes its component programs.

GIPSA's Grain Inspection Program plays a critically important role in facilitating the marketing of U.S. grain and related com-

modities. We provide the U.S. grain market with Federal quality standards and a uniform system to apply these standards. We partner with state, private agencies and laboratories to bring accurate and affordable services to American agriculture from the producer to the processor and the exporters.

By serving as an impartial third party, GIPSA assures that the standards are applied and weights are recorded in a fair and accurate manner. We bring discipline and integrity to the marketplace. Our presence, which directs through the use of the standards methods for the commercial industry, improves the marketing of U.S. grain and oilseeds from our nation's farms to the domestic and foreign buyers.

We carry out the important program under the authority of the Grain Standards Act for most grains and oilseeds and the Agricultural Marketing Act for rices and processed grain products. Under separate correspondence, the department will be submitting for consideration by the Congress a draft bill to amend the United States Grain Standards Act to reauthorize Grain Inspection, Packers and Stockyards. The current authorization expires at the end of this fiscal year.

Today's grain markets handle a greater diversity of grain quality than ever before. We must be efficient for American agriculture to remain competitive in the global market. The service we provide through the grain program helps make this happen. We are addressing the grain quality concerns of our international customers. We are establishing a biotech reference lab to improve the accuracy and consistency of the biotech detection methods. We are improving the efficiency and the quality of inspection in our weighing services through automation. Finally, we are working with our trading partners around the world as they develop their own grain standards and grading systems.

Our Packers and Stockyards Program provides financial protection, promotes a fair business practices and competitive marketing environment for livestock, meat and poultry. Our programs guard against deceptive and fraudulent practices affecting the marketing of meat animals. To carry out this task, the Packers and Stockyards Program administers the P&S Act of 1921 and also carries out the Secretary's responsibilities under the Food Security Act of 1985, which permits states to establish central filing systems.

Packers and Stockyards personnel work continuously to respond to the adapting conditions and changes in the dynamic and complex industry. Our reorganization of P&S programs will allow us to better address the structural changes in the industry and the concentration issues with increased expertise. This will allow us to reduce our Washington staff from 28-percent of our total personnel down to 18-percent and put those resources in the field.

Today we have 83 different investigations going on in our P&S program, plus all of the other requirements we perform. Since reorganization, we have shifted our focus to procurement, increasing the frequency and sophistication of our investigation and surveillance efforts to ensure that slaughtering packers are actively competing for slaughter requirements and not engaged in illegal trade practices.

In addition, the Agency is conducting a semi-annual investigation of hog slaughtering firms that use electronic evaluation devices as part of their purchasing program to ensure that these devices are used in a fair and accurate manner in determining the value for producers.

Over the past 5-years since I have been administrator, we have conducted over 9,300 investigations. We have found about a third of those investigations were violations of the P&S Act. The largest number of these were resolved by our personnel and formal action was only taken on approximately 200 cases, resolving these decisions and orders against 290 individuals and firms for violating the P&S Act, resulting in civil penalties and cease and desist provisions involving unfair trade practices and anti-competitive activities. Small and medium-sized producers have been the big beneficiary of these actions.

Structural changes in the livestock industry have challenged the job of the Packers and Stockyards. High concentration, forward sales agreements, production contracts, vertical integration have raised major concerns about competition and trade practices in the livestock and procurement by meat packers and poultry processors.

Concentration in the meat packing industry is relatively high and has been growing. The four leading packers in 1978 increased their share to 81-percent of the steer and heifer slaughter. The hog slaughter in 1998 increased to 56-percent. In addition, both slaughter and production of livestock have become more concentrated in the geographical regions.

A few of the present initiatives that we are involved in—this past year we developed a rapid response team. That team has responded to South Dakota and Missouri in July and September, to respond to producers' concerns about ensuring adherence to the P&S Act. A new price discrimination law was passed in these states. Packers reacted in a manner advised by their counsels. We were there; we interviewed producers. We still have some inadequacies we feel that need to be addressed. Also, a small rapid response team was on the scene last week handling a poultry trust case in Nebraska and Iowa.

We also have an initiative to develop a hog contract library through monthly contract use reporting. This library will be housed in the Des Moines, Iowa office. It is called for by the Mandatory Livestock Reporting Act of 1999. USDA is establishing this library of contracts by hog packers to producers for the purchase of hogs. The department will collect and summarize information on the number of hogs committed to the contract, and release this information in a public manner.

USDA filed a formal complaint against Excel, alleging that the firm violated the Packers and Stockyards Act by failing to disclose to producers a change in the calculation of the lean percent for hogs purchased on a carcass merit basis. As a result of this change in formula, Excel paid producers a lower price for hogs. The hearing is scheduled for February 29.

USDA also filed a formal complaint against Farmland National Beef Packing, alleging that the company violated the P&S Act by failing to make bids or purchase cattle from a small feedyard in Central Kansas after the feedyard had published an article critical

of marketing alliance procurement procedures used by Farmland. Farmland, we felt, is subject to unreasonable prejudice, disadvantage and retaliation against this feedyard.

Now I would like to discuss two legislative initiatives that would enhance GIPSA's ability to protect producers and growers. The first legislative initiative would be to amend the Packers and Stockyards Act to establish a statutory dealer trust for the benefit of livestock producers. USDA has drafted and submitted to Congress a bill for review.

As you know, Mr. Chairman, this provision was included in the 1996 farm bill by your initiative but was blocked in the House during the conference committee.

Dealer failures represent a significant amount of unrecovered losses in the livestock marketing chain. For fiscal years 1994 through 1998, dealer failures averaged fourteen per year in this country. Amounts owed to livestock sellers averaged a little over $3 million per year. Of this amount, only 25-percent was recovered. During the same period under the packer trust, nine packer failures resulted in a pay-out of close to $2 million from the packer trust program and approximately a 95-percent recovery rate. A dealer trust for cash sellers of livestock would minimize the losses suffered by livestock producers because of dealer failure to pay.

Our second legislative initiative would be to amend the Packers and Stockyards Act to grant USDA enforcement authority over contract poultry production. This proposed legislation was introduced last year in the House by Representatives Kaptur and Emerson.

Under Section 202 of the Act, packers and live poultry dealers are prohibited from various unfair, deceptive and unjustly discriminatory practices. A live poultry dealer is defined as a person engaged in the business of obtaining live poultry by purchase or under a growing agreement for the purpose of slaughter or for sale to others for slaughter.

Enforcement of Section 202 against a packer is accomplished through an administrative proceeding before an administrative law judge. Enforcement against a live poultry dealer can only be accomplished by referral to the U.S. Attorney's Office and filing in a Federal court.

Section 203 of the Act, which deals with administrative enforcement, specifically refers to packers and not live poultry dealers. We believe this regulation of the activities of live poultry dealers would be more efficient if the Act was amended to provide for administrative authority. It is difficult for us to do the task and have the responsibility without the authority.

We look at approximately three-hundred poultry complaints a year.

Thank you, Mr. Chairman, for allowing me to provide this oral testimony.

[The prepared statement of Mr. Baker can be found in the appendix on page 80.]

The CHAIRMAN. Well, thank you very much, Mr. Baker, and thank you for your specific legislative suggestions, which are important and which will certainly be a part of this hearing.

Mr. Dunn, it is good to have you back at the Committee. Would you please proceed?

STATEMENT OF MICHAEL DUNN, UNDER SECRETARY FOR MARKETING AND REGULATORY PROGRAMS, U.S. DEPARTMENT OF AGRICULTURE

Mr. DUNN. Thank you, Mr. Chairman. It is good to be here and I appreciate the opportunity to briefly address you on the concerns.

I think what Senator Feingold outlined, the dramatic changes that are taking place in the livestock sector, actually all of agriculture, the marketing chain, really does put a tremendous burden on producers, the administration and members of Congress. I know Senator Grassley and I were in Iowa listening to concerns of producers on concentration issues.

As Mr. Baker outlined, Packers and Stockyards is designed to look at unfair trade practices and in some ways a bit of the concentration area, but we share—the majority of that is in the Department of Justice. Mr. Joel Klein, who heads up that division, the Antitrust Division of Justice, has recently named Mr. Doug Ross as his new assistant for the agricultural sector. We look forward to working closely with Justice in this particular area.

Let me outline just two more areas that the department is working in this arena. Mr. Chairman, Congress passed last year the Livestock Mandatory Reporting Act and has asked us to implement that. Under the Agriculture Marketing Service, we have put together a multi-agency task force to implement that. We are well on our way to doing that. We hope to have by this summer operational those price reporting regulations out and operational that Congress has mandated.

A second area that the Ag Marketing Service is working on, again working across the board in the department, is putting together a group to look at contracting because we hear over and over again concerns by producers about contracts that they have gotten into and what has happened in those contracts. We are really calling this a right-to-know initiative and we think this is extremely important.

Mr. Chairman, we appreciate this Committee taking this overall look at the tools that the department has and the need for changes in both legislation and regulation. We look forward to working with you and the Committee. Thank you.

The CHAIRMAN. Thank you very much.

We have been joined by the distinguished senator from Idaho, Senator Craig.

Let me begin the questioning and then I will ask my colleagues in turn to join me in that.

Mr. Baker, you have made suggestions for legislation. Tell me, is this in draft form and what sort of consultation have you had with staff of either a Senate committee or House committee with regard to reauthorization or the extended authorities that you seek?

Mr. BAKER. The reauthorization will be coming forward to you from the department. In other words, it has cleared the department and is ready to come forward to you.

The two bills are in draft form and they have been submitted. Livestock dealer trust has been submitted already this past year to you. Also, the administrative authority over poultry companies has been submitted; it has been introduced in the House by Congress-

woman Kaptur. So those two bills have already been submitted. The reauthorization will be forwarded to you real shortly.

The CHAIRMAN. Now, the Congress last year, as you have cited, the Mandatory Price Reporting. How are the guidelines for that or the administration of that proceeding at this point? What can we anticipate as we have oversight of how that is working out?

Mr. BAKER. Let me talk just a minute about our part of it because I have tried my best to keep our folks out of it. We have the part about the contract library for hogs and that is clearing the department as we speak. We want to have a library of all contracts offered by packers to producers. They will be on file in Des Moines and it will be open to the public. We will have confidential restraints that we will hold confidential in it but we will release those types of contracts to the public so they can keep better informed, according to this law. It was mandated under the Mandatory Price Reporting Law. That is part of it.

We will also secure the numbers of hogs that are under contract that are expected to be marketed in the next 6-months and within the next year and we will release those as we get them to the public. The purpose of this is to keep the public better informed. I would like to see it and we have an initiative to try to get it extended into poultry and also into cattle. If you are going to do contracting, you ought to have to file it with somebody. There ought to be some checks and balances about the contracts. I will let Mr. Dunn——

The CHAIRMAN. Mr. Dunn, can you give a broader overview of the rest of the department, how it is proceeding?

Mr. DUNN. Yes, Mr. Chairman. As I said earlier, we have convened a group down at the department to address the various provisions and we have broken it out to nine different sections, in essence, and I will go through quickly for you where we are on those nine sections.

The CHAIRMAN. Very good.

Mr. DUNN. On the Livestock Marketing Report, which is the major sections, 211 to 256, those are the ones that $4.7 million were appropriated last year from the appropriators most of the provisions and those are the ones that we will have out and operational by this summer.

Sections 257, which is the retail purchase price reporting, the Economic Research Service is working on that. They unfortunately did not get appropriations and are looking for appropriations to be able to implement that section.

Section 913(b) is the Export Marketing Report. We are working with Foreign Agricultural Service on that and they were appropriated $50,000 to do that this last appropriation period, so they are working on getting those out. We expect to have final OMB clearance by mid–April on those.

Section 922, which is the export certification for meat and food products, food safety and inspection service [FSIS]. They requested $2 million for appropriations in fiscal 2000 for that. They did not get that so unfortunately, we do not have the appropriations to go forward on that.

Section 923, beef and cattle import data, APHIS is working with FSIS on that. Although we were not budgeted any money, we think

that we can begin to put that together a program with the current budgets.

Section 932, which is the improvement of the Hogs and Pigs Inventory Report, National Agricultural Statistics Service [NASS] is working on that. They requested $500,000 for appropriation, did not get that, so we will probably be seeking appropriations on that.

Section 932(a), which is barrow and gilt slaughter, FSIS again requested a little over a million dollars for fiscal 2000 and was not appropriated that money. They are ready and willing to get started on that as soon as appropriations are made.

And Section 933—this is number eight of the nine—average trim loss correlation studies and reports, the Agricultural Research Service and Animal and Plant Health Inspection Service [APHIS] are coordinating on that study and will get started on that.

Then finally, Section 934, Swine Market Contract Library, the Grain Inspection, Packers and Stockyards is working on that and Mr. Baker answered where he is on that earlier.

The CHAIRMAN. Well, I appreciate your parceling all this into these parts but obviously, as you have cited, in at least four instances or maybe five, appropriations did not happen or they are deficient and as a result, the entire Act situation is being frustrated, I would guess. We had the best of intentions here in Congress but, on the other hand, somehow communication with the appropriators, with the administration, just has not made it.

I do not want to try to make a broad editorial comment because I know this has already been a subject of some distress at the department, as well as with those on this Committee, including myself, who strongly favor this legislation and turned heaven and earth to get a consensus to do it and I am just wondering how much of it is going to get done under what you are describing.

Mr. DUNN. Mr. Chairman, I thank you and all members of this Committee that worked very hard assisting the administration on appropriations in this effort.

This whole aspect of transparency in the price reporting seems to be one of fundamental need out in the marketplace.

The CHAIRMAN. Yes.

Mr. DUNN. The producers' need more price information. We have zeroed in on the Livestock Marketing Report, what used to be voluntary market news, making that mandatory so that producers have the same type of information that packers have. That, in our consultation with livestock producers, is what they said was their number one priority.

We did get the $4.7 million for that and we are going forward with that and we will have that operational this summer. I believe that will take off a lot of the pressure that we are getting for information out there. That seems to be the section that producers have told us that they wanted to get out.

The CHAIRMAN. Well, let me just say I appreciate the specifics because we are going to ask staff to work with you and with the department and see if we cannot find where the money can be found. This has proceeded on for weeks with reports of lack of appropriation or lack of activity and I suspect my colleagues on this Committee join me in saying that one of the values of these oversight hearings is simply to find out where the chinks in the armor

are. I think we have identified some of them and you have pointed out the priorities certainly of the Act and that clearly is true, but the checkerboard pattern of activity is disturbing—to you, as well as to us. So we really need to zero in on how we can get on with it and I welcome that opportunity.

Mr. DUNN. What we will do, Mr. Chairman, is proceed on with drafting of regulations, even though we do not have the resources to do the implementation.

The CHAIRMAN. That would be a good idea. Let's at least get the department's work in terms of rulemaking, the regulations, done, quite apart from then the application in the field which, of course, is increasingly urgent.

When do you suppose that in the case of the $4.7 million, that area of your activity, there will be some reports that will be available to producers? The second quarter of this year or what sort of timetable do you see happening?

Mr. DUNN. On an optimistic schedule, second quarter of this year we should be able to begin getting some of those reports out, but I would hope that we would have it fully functional by this summer.

The CHAIRMAN. I see. Let me just ask one final question.

Anticipating the testimony we are about to hear from Professor Paarlberg and Foster, they have written a paper that I think is remarkable, trying to take a look at the concentration that we are all talking about today, but suggesting a remedy; that is a much larger degree of cooperation, at least in the hog industry, among producers. They make a suggestion in their paper that if we had enough cooperation and a large enough cooperative of 300,000 to 500,000 head of livestock could be aggregated to affect one or 2 days of the market, that this might begin to bring in a different sort of balance in terms of price-finding in the situation.

Now that has been hard to come by in the pork industry, with many independent producers and many not really wishing to get all that cooperative and, as a matter of fact, wanting to be very independent.

I come from a tradition—there is no way you would know this but my dad and my grandfather were livestock commission people. We were a commission company for 40-years at the stockyards. It was our bread and butter and that stockyard is just gone. It is a sort of part of the restructuring and the evolution we are talking about.

So it is different but the dilemma is also different in both degree, as well as the intensity, and that is what has brought a great deal of interest to this issue.

I just wonder if you have any comment generally about the cooperative movement, at least the extent that the professors have suggested as one remedy to the bargaining situation. Do either one of you have a thought about that?

Mr. BAKER. I haven't read the paper, so I cannot comment on it.

The CHAIRMAN. Very well.

Mr. DUNN. Certainly, Mr. Chairman, this is an area that the department has always advocated—Under Secretary Jill Long–Thompson has worked very hard in this area in developing from your home state the cooperative group and has worked with the

Small Farms Commission at the department to develop a concept of cooperative marketing.

Again what we have found is a lot of the producers are very, very good at production but they seem to begin to need further information when it comes to the marketing side of it. That is again why we have put together a task force in the department to look at contracting and, as I termed it earlier, a right-to-know initiative so that producers will have the department or somebody else to fall back on to look at how you would go about contracting, how they can maximize their return. And in many cases putting together some type of alliances or cooperative operation seems to make a lot of sense, to be able to maximize the return to producers.

The CHAIRMAN. The distinguished ranking member has arrived. While you are sorting through your papers, let me call upon Senator Baucus.

Senator HARKIN. That sounds like a good idea.

The CHAIRMAN. Then you will be all ready, up to top speed.

Senator Baucus?

Senator BAUCUS. Thank you, Mr. Chairman.

Mr. Secretary, the Paarlberg piece—I just glanced at it—is quite interesting and one cannot leave it without feeling quite strongly that those authors at least think that there is a significant problem and that concentration probably is resulting in downward pressure on prices to producers. I think this is a hog study but my guess is that it would apply to other livestock industries. There is not much doubt in their minds. I do not want to put words in their mouths but I got the feeling that they think it is significant and it should be addressed, the problem.

They do say there are two ways to address it, and that is basic antitrust breaking up and second is, as the Chairman suggested, a lot more marketing power in the hands of producers. And we all know both options have unique difficulties.

I am just trying to get a sense of how much the department thinks it is the problem and how aggressively the department is really working on this. Can you give me a feel about first, the degree to which you think this concentration is a significant enough problem to warrant significant action? That is, producers, as a consequence of concentration, are paid lower prices for their product? Again it is not the sole reason but do you think it is a major reason, sufficient enough to warrant doing something significant about it?

My concern, Mr. Secretary, is that this issue has been around a while and here it is, several years since it has been around. I know a lot of producers are getting kind of frustrated. It's the old thing, a lot of talk. And I must be candid with you in saying that so far, I hear a lot of talk from all the way around, both Congress, frankly, and the administration, but I do not see a lot of action. Do you think the problem is great enough to warrant action, significant action?

Mr. DUNN. Senator, any time we get down to $8 hogs, we have a significant problem in rural America. And yes, we need to take action.

Now when Senator Feingold was up here, I think he outlined the problem that you have in determining what caused that low price.

Is concentration the major cause or is it a consequence? The whole aspect of causality is something that we have got to have empirical data on.

Senator BAUCUS. But we have had 3-years on this. You have been looking at this question for 3-years. What is your gut guess?

Mr. DUNN. My gut guess?

Senator BAUCUS. Your gut guess.

Mr. DUNN. As Mike Dunn?

Senator BAUCUS. Mike Dunn.

Mr. DUNN. I think it contributes to it.

Senator BAUCUS. But is it a significant contribution, significant enough to warrant significant action?

Mr. DUNN. I think it is significant enough that the Congress and the administration need to work together to find out how can we address this problem. So yes, it is significant.

Senator BAUCUS. Now, what about this study I just learned of? It is by the Western Organization of Resource Councils. They submitted a petition asking GIPSA to participate in a rulemaking. The comment period has run. As you know, the comments were fifteen to one in favor of a petition for rulemaking to the Secretary, asking that USDA use its authority under GIPSA to restrict the way packers use captive supplies. You know this is also peer-reviewed and my understanding is the peer review agreed with the conclusion.

Now I hear that attorneys and economists at USDA are not convinced yet that the cause has been established. To be quite candid, it sounds to me like a lot of timid, tepid, fearful people are afraid they might make a decision, might be held accountable.

What standard of causality is the department asking for? Is it the criminal standard of beyond a reasonable doubt? Is it the civil standard of the preponderance of evidence? And I must ask a deeper question: why do you even have to prove cause? If it is your judgment, as you just said, that it is a factor and it is a significant factor, why not just proceed and perhaps proceed on a pilot basis project if you are a little nervous about this. See what works; see what does not work.

We have to do something here. When I saw this hearing scheduled I almost decided not to come. I thought it would be a waste of time because there has been so much talk on this issue. But I have a responsibility to keep on plugging away, keep trying. We have two choices in life: try or do nothing, and I am still going to keep trying to do something about this responsibly.

I did mean what I said about unintended consequences, but we have to move, Mr. Secretary. We have to move and I am just asking you what we are going to do to move.

Mr. DUNN. Senator, let me address the Western Organization of Research Council's petition. What they have petitioned us to do is change the way people can do marketing. It is a fundamental change, saying that certain people would not have marketing rights that they had before.

So this is really a major step and something that we felt we needed to get a lot of comments on, we had to have good, strong and careful data before we could go forward with that. We published that proposed regulation, that request for proposed regulation, and got comments on it. We had a peer review on a study and

the Secretary pledged to the Western Organization of Research Council that he would not make a decision on that until he had that peer review and then he had an opportunity to sit down with them and go over that peer review.

We have contacted them even this last week to try to set up that meeting, to sit down with them so that the Secretary can go over that peer review with them and see what direction to go.

Senator BAUCUS. But do you feel you have enough authority through the department to take sufficient action currently?

Mr. DUNN. With respect to——

Senator BAUCUS. With respect to the general question of concentration.

Mr. DUNN. On the area of concentration, Packers and Stockyards is a very, very powerful law but it is not the Clayton Act and it is not the Sherman Act.

Senator BAUCUS. We are told that neither the Clayton Act nor the Sherman Act, as currently written, allow Justice to take any action.

Mr. DUNN. I would have to defer to Justice.

Senator BAUCUS. No, they cannot prove collusion. Bigness itself is not a sufficient reason for action under either act, according to Justice. So they say they do not have the authority. And you are saying what?

Mr. DUNN. We do not have the authority to act on concentration issues. Justice has that authority.

Senator BAUCUS. They say they do not have it. Current law does not allow them to proceed because they cannot "prove collusion." They have not investigated as to whether they can prove it or not but on surface examination, they feel they cannot prove it.

Mr. DUNN. I think that is one of the reasons why Mr. Klein proceeded the way he has, appointing an Assistant Attorney General to assist him in that arena. We do have—we have signed just this last year a memorandum of understanding with Justice so that we can bring to bear all the resources that we have at the department to assist them on doing that investigation. But at this time, if you cannot prove the collusion is there, they cannot go forward.

If the Congress feels that we need to do some type of breaking up, certainly you can mandate that we do that.

Senator BAUCUS. All I am saying is there has been a lot of talk all the way around this thing and my gut feeling is that concentration is a very significant reason why, at least in some industries, say in livestock, prices are low to producers—not the sole reason, but a significant reason, and significant enough to warrant very definite action. I just want you to keep working on this until we find a way to do this in a fair way, responsibly.

There are a lot of values here, too. It is not just economics. It is the values of open space, keeping farms in the family, the values of small farms. And I think, frankly, it is in the interest of a lot of packers to want to make sure that more producers are around, ultimately. Maybe at this point, 2000, February 1, it might make sense for them to keep squeezing more out of the producers but pretty soon there is not going to be much left and I would urge packers to work with producers to find some ultimate way to help producers get more out of their efforts.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Baucus.

Let me just say I did not want to interrupt——

Senator BAUCUS. I apologize for taking so long.

The CHAIRMAN. Well, they were good questions.

Let me say in fairness now to all senators, we have a five-minute limit on the question round and that is going to be true for witnesses, so that we are able to hear from everybody and have the proper questioning.

I am going to call now on Senator Craig, who arrived a while back and has not had an opportunity to speak. Senator Craig?

STATEMENT OF HON. LARRY E. CRAIG, A U.S. SENATOR FROM IDAHO

Senator CRAIG. Mr. Chairman, I was here to listen and not to speak. I think this is an issue that all of us are growing increasingly concerned about. I have been frustrated, as I think Senator Baucus has expressed his opinions.

I come from a ranching background and when you see numbers drop, historically you see the pattern of prices increase, and that simply has not occurred out there, while it appears that packers have made exceptionally large profits.

There is a concentration. I am not quite sure that the models that we are using to look at the concentration give us a fair image of what is current in the market. Those are old models and the market is a new market. And that is going to be some of the responsibility of Congress, Mr. Chairman, and I must say I appreciate these kinds of hearings. I hope that they become increasingly probative.

While certainly the marketplace can respond and I am going to read the effort of these professors that are before us who analyze and are making recommendations, that there are ways that the market can respond, but they may need some assistance, and that assistance probably has to come from the Congress of the United States. So I thank you very much.

The CHAIRMAN. I thank the senator.

I will call now on Senator Harkin for his comments and questions.

STATEMENT OF HON. TOM HARKIN, A U.S. SENATOR FROM IOWA, RANKING MEMBER, COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY

Senator HARKIN. Thank you, Mr. Chairman.

Well, count me among the previous two that are frustrated. I must say, Mr. Chairman, I commend you for holding this hearing, these comprehensive hearings on the Packers and Stockyards Administration and on GIPSA.

I sense the same kind of frustration among Iowa farmers, that Senator Baucus and Senator Craig have just related. During the recess period I spent a lot of time obviously out in Iowa, in the Midwest, and this is an issue of tremendous concern. That is all I hear, about the concentration that is happening in the livestock industry.

Now having said that, I would say to my friend Senator Baucus, George Bernard Shaw once left England and he spent the better part of a year in New Zealand. He came back to England and someone asked the great playwright, "How did you like New Zealand?" He thought for a second and he said, "Well, all together, too many sheep."

Senator BAUCUS. Why are you asking me that?

Senator HARKIN. The reason I say it is because——

Senator LEAHY. We are all waiting, Tom. We are all waiting.

Senator HARKIN. We just had too much of a supply, too many hogs, and we had too many cattle and stuff like that. But the point is we expect that to happen but while it is happening, when the supply as big and the packers had the contracts out there, you see this big shift in the structure.

So when we get back to a more even keel, we are going to find ourselves in a whole different lay of the land than we ever had before, and that is what really bothers me, is that during a period of time when we had low prices because of oversupply, we found the industry moving to consolidate very rapidly in all parts of the country.

I was just looking at some of the data there about how much we have concentrated just since 1981. I think you find, I think in cattle it has gone up to about 80- some percent now and I think in hogs it is about 56- or 60-percent, somewhere in that range right now. It is not quite as bad in hogs as in cattle.

I guess you have to ask the question: is that per se bad? Well, I think economic concentration per se is bad. It is just bad for the economy. It is bad for any kind of competitive structures out there. And it destroys any kind of initiative out there for younger people to perhaps try innovation and try to do different things to become even more efficient.

Again we have been talking about this. I have been on the Ag Committee for twenty some years. We have been talking about this—we talked about this in the 1980s and talked about it in the early 1990s and we just keep talking about it, as Senator Baucus said. We just keep talking about it and I just wonder if we are not at a point here where it will be too late to do anything about it. It will be a fact, a fait accompli, it will be done and there is not anything that we are going to be able to do about restructuring at that point in time.

Change is inevitable, in all facets of life and certainly in agriculture, and I do not mind changes, but changes that lead to lack of competition and a structure of monopoly practices is not change for the better. I just do not see in any that is going to be any kind of change that helps our farmers and ranchers at all and helps us in any way to be even competitive overseas.

So again, I am hopeful that we can think about changes that we might make in the Packers and Stockyards Act, for example, to define what anti-competitive practices are under Packers and Stockyards. Do we know? Jim, I do not know. I understand that we do not really have rules that really define what anti-competitive practices are under Packers and Stockyards Act.

Mr. BAKER. The way we define it is when it brings harm to other people. In other words, when people have been harmed, it is anti-

competitive. In other words, it has harm, a direct effect in the marketplace. That is how we define it.

Now I think most of the talk has been on antitrust up till now and P&S—we yield to Justice on antitrust matters. We look at the anti-competitive measures and Senator Harkin, we bring several cases on anti-competitive matters. You know, turn-taking, this type of thing is a violation that we bring. Failure to compete.

Senator HARKIN. Well, I will say one thing has happened. I guess Mr. Klein has put someone in the Department of Justice that is focussed just on agriculture. Is that person in place yet?

Mr. BAKER. Yes. He is here now.

Senator HARKIN. That is good. Is he coming up here?

The CHAIRMAN. Not today.

Senator HARKIN. We have to ask him what he is doing.

Lastly, I understand that there was a proposal put forward, shifting from livestock now to grain, there was a proposal put forward last year by USDA that would offer interest subsidies to export elevators desiring to install cleaning equipment as an effort to encourage shipment of cleaner grain overseas.

I want to know more about that proposal. Mr. Chairman, I think that is something we ought to look at. Obviously, one of the things that can affect the price of an export is to convince buyers that our product is higher in quality than our competition. So I think we ought to look at this very carefully and I think it has a lot of merit to it. Are you still pushing that idea?

Mr. BAKER. Yes, Sir, but Dave Shipman is with me and he addressed the industry last week. Let him tell you where the industry is coming from and a little bit about the grain cleaning, what our update is briefly.

Mr. SHIPMAN. On November 29 the department published in the Federal Register a proposal to use some Commodity Credit Corporation [CCC] funds to help fund cleaning at export facilities. And just last Friday, on January 28, we had a public hearing at the department where we had importers from Latin America and Africa come and talk to us. We had producer groups come and talk and present their opinions on it and we also had a number of exporters, those from the Pacific Northwest that have already invested in cleaners and some representing the Gulf Coast area where they have not.

There was really a great deal of contradiction in the statements that were made and we are now kind of filtering through all of that. We will be meeting with Tim Galvin in Foreign Agricultural Service [FAS] later this week to further talk about the issue.

In general, I think the exporters and the grain industry at large expressed concern about government intervention, that the market economics should drive the installation of cleaners. That is what occurred out in the Pacific Northwest. There was a large enough demand coming from the Pacific Rim for cleaner product and the market responded and made those investments.

They do not feel they have seen that large enough demand yet in the Gulf Coast, so there was concern expressed about letting the market——

Senator HARKIN. I see that they do not complain when we promote Public Law 480. They do not complain about that. They do

not complain about the Market Assistance Program. I mean why would they be complaining about this as some interference in the market? That went right by me. I do not understand that one at all.

Mr. SHIPMAN. And then the producer groups expressed other concerns.

Senator HARKIN. If they do not want to install the cleaning devices, the heck with them. We ought to look at offering them some interest subsidies or something and if they want to do it, fine. If they do not, let them go.

Mr. SHIPMAN. There is going to be further discussion in the department on it. One suggestion was made that we should be looking at changing the standards rather than offering financial incentives to make the change. So there is going to be further discussion in the department later this week.

Senator HARKIN. Well, I do not know enough about it to comment on that. I mean maybe that is the better way to go. I do not know, but I think it is something we ought to take a look at.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Harkin.

Mr. Shipman, I read some of the testimony of that hearing and you are correct that people were all over the place. Although I would suggest Tim Galvin and others, I thought, conducted the hearing in a very civil and temperate way, as is their custom, but to say the least, that is one that will require a lot of resolution of very interesting points of view.

Let me call now upon Senator Roberts, who has patiently waited for an opportunity to intervene this morning.

STATEMENT OF HON. PAT ROBERTS, A U.S. SENATOR FROM KANSAS

Senator ROBERTS. I do not know about intervening, Mr. Chairman. I want to thank you again for your leadership in holding this hearing. We have heard a great deal of frustration. This might be described, as opposed to an Ag Committee hearing, as a Frustration Caucus on this issue.

I apologize for being late. I apologize to the witnesses. As a matter of fact, I was meeting with the Kansas Hospital Association and one of their comments was that we have to really worry about the issue of concentration and closing down rural hospitals in regard to regional hospitals. I said, "It is really ironic; I am going to a hearing on concentration on agriculture and we have it all across the economy in our society."

And thank you for holding the hearing, Mr. Chairman. You are right on top of it, as usual.

I think rather than simply read my statement, there are just a couple of highlights here.

Obviously people are extremely fearful and very frustrated. We have extremely low prices, a strong dollar, a collapsed foreign market due to what we call the Asian flu, but that is true in a lot of areas of the country. So we should expect, when we are going through this, that this long-time problem that has been described by Senator Harkin would become a matter of real concern and fear.

I know the Clinton administration has announced that a special position has been created within the Department of Justice to deal with mergers and anti-trust issues. I apologize for not doing my homework. Who is that?

Mr. DUNN. Doug Ross is his name.

Senator ROBERTS. I am sorry?

Mr. DUNN. Mr. Ross.

Senator ROBERTS. Is Mr. Ross here?

Mr. ROSS. Yes, Senator. I am Douglas Ross.

Senator ROBERTS. So you are the guy. Welcome.

Mr. ROSS. Thank you, Sir.

Senator ROBERTS. I guess condolences or something. I think that is a very important move and we look forward to working with you.

I would like to make just a couple of points, Mr. Chairman, and that is that we are going to have to work with the Judiciary Committee. The Ag Committee really does not have the primary jurisdiction but we have the keen interest, it is our people involved, but it seems to me we have a lot of frustration but not much expertise. We all know we want to do something but we are not quite sure what it is and you do not want to make it counterproductive. You know, beware of the law of unintended effects. I am sure that Senator Baucus did address that.

Just a couple of questions. Do mergers actually reduce the producers' marketing options and reduce their ability to obtain a fair price? You ask that question out in Kansas and the answer is going to be what—80, 85, 90, maybe 100-percent yes.

If we block or place a moratorium on mergers, will it hinder or eliminate, however, the ability of U.S. companies to compete in the world marketplace? Is this beneficial to our producers? If we block all mergers, are we actually limiting the producers' ability to compete in the marketplace?

Everybody on this Committee as long as I can remember has told producers they need to participate in value-added agriculture. Will moratoriums keep this from taking place? Or can you devise a law that would exempt those kinds of things? I do not know.

Four Western Kansas farmer-owned cooperatives joined with Cargill late last week to announce they have come together to form a joint company that would allow them to ship their grain more efficiently and return higher profits to producers. How will legislation affect that?

Same thing in regard to livestock with U.S. premium beef in Kansas.

You know, these are questions that we should not take lightly.

And then this is not only in agriculture. We have it in banking, energy, and technology, as well, so I think we have to take that into consideration.

Now I have publicly stated several times that if the administration, the Department of Justice and the Department of Agriculture and the Congress really believe that new legislation is needed or certain areas need to be addressed, that the administration and the Department of Justice and the USDA should put us on notice and provide us with the necessary input and guidance, put something on the table, and I know you are trying to do that and I know you discussed that with your testimony.

But Mr. Chairman, like Senator Harkin has indicated, this is a very big problem and if we do not act, states will. The state legislature of Kansas is considering a package of bills determined as a result of independent and bipartisan hearings of people who went around themselves, members of the state legislature, on the merger question and the concentration question. And Kansas could act. I am not sure what they are going to do.

But we have a lot of laws on the books here that deal with national issues and state issues and I remember all of our efforts to provide uniform tolerance in the food safety arena. Otherwise, you end up with a hodgepodge. You know, Iowa is going to pass a bill and Kansas is going to pass a bill, South Dakota is going to pass a bill. Illinois may not pass a bill. That is going to be terribly counterproductive.

So it seems to me that we ought to get some degree of cooperation and understanding on where we are going to go. And with all due respect, I do think that first starts with the administration in regard to what you would like to see in terms of legislation, and I will stop at that point. My time has run out. Thank you for the hearing. I am interested in the testimony.

The CHAIRMAN. Thank you very much, Senator Roberts. You make a good point with regard to state activity. Kansas is not unique in that respect and clearly our need for a colloquy with the administration on its organizational attempts is imperative.

Do you have a further comment on that?

Mr. DUNN. Yes, Mr. Chairman, because I, too, am concerned about this hodgepodge that is going on. We at the department have contacted the National Association of State Directors of Agriculture and have talked to attorneys general and we are going to commence having a series of meetings with them. These will be working sessions designed to discuss what state legislation exists versus Federal legislation—where we are, where we see cracks and where is the safety net not buoyed up.

So I think you have hit on a major concern of ours, that we are getting these hodgepodges of state legislation and it is going to be very, very hard to coordinate commerce with that type of quilt blanket throughout the Nation. So we will be working very closely on that, Senator Roberts. That is a good something.

The CHAIRMAN. Thank you very much.

Introducing our next questioner I would comment, as a point of history, this is the first hearing of the Committee in the year 2000 and it is appropriate that the gentleman whose picture appears on the wall in the corner is here. Many of you have not attended a hearing before should note that this is one and the same with the senator who is here. It is, in fact, still a very good likeness, Senator Leahy. It is intimidating. Senators should look at that portrait. We are grateful you are here, as always, Pat.

Senator CONRAD. Mr. Chairman, might I just inquire, is there any chance we could have a vote in the Committee on whether that picture continues to hang there?

Senator LEAHY. No, no, no. It would require unanimous consent.

The CHAIRMAN. No vote.

STATEMENT OF HON. PATRICK J. LEAHY, A U.S. SENATOR FROM VERMONT

Senator LEAHY. That is called the Dorian Gray memorial picture.

Mr. Chairman, I want to thank you. I have said before that one of the great joys of being in the Senate is the friendship you have always shown me from the day you came here to the Senate and working together with you. The greatest honor I got was when you took over as Chairman of the Committee and rammed through the resolution to put that picture up there and to fend off the amendment to put numbers or a "Wanted" sign across the front.

When my daughter saw it she said, "Dad, looks good; who is it?" I said this is something that Senator Roberts and I were so happy to finally have a portrait of somebody who knew how to comb their hair around this place.

Senator ROBERTS. If the senator would yield——

Senator LEAHY. I knew that was a mistake right there when I said it.

Senator ROBERTS. All of us in the follically challenged caucus do appreciate the honor that has been bestowed upon you and if you would care to go over to 1302 in the sometimes powerful House Agriculture Committee, you will see that they hang people over there, as well.

Senator LEAHY. Not only have I been there but I have a copy of a beautiful program they had of that in my daily journal archives, with your portrait.

Senator ROBERTS. Bless your heart, Sir.

Senator LEAHY. I could use it.

I will just be very brief, Mr. Chairman. I said last year that I worry that our farmers and ranchers are too often at the mercy of a new kind of robber baron, the agricultural conglomerates who can do a sort of take-it-or-leave it offer to most producers. I said I really want to have more competition or the ability of more competition if we are going to have a healthy farm economy.

And I want to work with you, Mr. Chairman, and with Senator Harkin to see if we can get a comprehensive bill to increase competition to protect these family-sized farmers and ranchers from unfair competition from conglomerates.

I am sorry that another committee takes me out of here but not only will my staff be here but I will be looking at this transcript and I will submit questions for the record because we have this case where the agribusinesses are enjoying record profits as they become more concentrated, but agricultural producers in most states are suffering severe economic depression with no end in sight.

When we met last year I said it was the agricultural movement in the late 1800s that played a pivotal role in the passage of the Sherman Anti–Trust Act and many farmers today face the problems of these gigantic conglomerates.

I remember reading in law school when I went back what Judge Learned Hand said in the Alcoa case. "It is possible because of its indirect social and moral effect to prefer a system of small producers, each dependent for success upon his own skill and character, to one in which a great mass of those engaged must accept the direction of the few."

So Mr. Secretary, we may want to be looking at ways to get more power to you to act against unfair or unjust or deceptive business practices.

We have had agricultural trusts before. In the 1800s American Sugar controlled 85-percent of America's sugar refinery. Standard Oil, of course, had 90-percent of our oil production. There were cotton oil trusts, sugar trusts, linseed oil trusts. There was even a whiskey trust. I am not sure, but then the Irish showed they could produce better whiskey in Ireland.

And I would leave this question for you, Secretary Dunn. Suissa Foods of Texas, I understand, has bought about 70-percent of the formerly independent dairies in New England and had a buying spree in other parts of the country. And I know that the Justice Department was worried about the problem that might cause, especially such things as the School Lunch Program, which affects us in all parts of the country.

Would you have your office put together a report on the Suissa acquisitions in the last 5-years, the markets affected, the volume of milk affected? I am concerned about what that might do to school lunches and just regular consumer costs, and if you could do that, Mr. Dunn, and get it to me, I would appreciate it.

Mr. DUNN. Yes, Senator, we will do that for you.

Senator LEAHY. And thank you, Mr. Chairman.

The CHAIRMAN. Thank you very much, Senator Leahy.

Senator Fitzgerald.

STATEMENT OF HON. PETER G. FITZGERALD, A U.S. SENATOR FROM ILLINOIS

Senator FITZGERALD. Thank you, Mr. Chairman. If I could ask for unanimous consent to submit my statement for the record, I would appreciate it.

The CHAIRMAN. So ordered.

Senator FITZGERALD. Thank you.

I have long felt that cooperatives were a great way for farmers to try and retain more of the value of their products at the farm level. I am wondering, do you have any statistics on, say, what percentage of farmers in this country would be involved in a cooperative? Would anybody on the panel know that?

Mr. DUNN. Earlier Senator Feingold talked a little bit about the number that the Dairy Farmers of America dairy coop had, but we can get that for you, Senator Fitzgerald, and we will supply that information of how much goes through coops.

Senator FITZGERALD. I would be interested in that.

The other question I guess I would have is does the USDA have programs in place that would foster more use of the cooperatives or help cooperatives along? Are there any policies in place along that line?

Mr. DUNN. Yes, Senator. Under rural development, Under Secretary Jill–Long Thompson has a division, Cooperative Development Division, that works in that arena. It works very closely with the rural business development group and they work very closely throughout the department with Ag Marketing Service that is under marketing and regulatory programs, as well.

Senator FITZGERALD. On a slightly different topic, has the department undertaken any activities to prepare for the challenges that are going to be arising with the new biotech crop marketing now that the farmers are being called in some cases to separate their crops and the like?

Mr. DUNN. Yes, Sir. We had requested in our appropriation this year appropriations to set up a reference lab in both Ag Marketing Service and a reference lab in Grain Inspection, Packers and Stockyards, and I will ask Mr. Shipman to answer specifically. We did get the funding for Grain Inspection, Packers and Stockyards; we did not get it for Ag Marketing Service, which would primarily look at fruits, vegetables, tomatoes and those things. But we did get it in the grain sector and I will ask Mr. Shipman to address that for you.

Mr. SHIPMAN. What we see in the marketplace is that we are starting to see more and more testing occurring to differentiate between conventional crop and biotechnology crop. So there was concerns about the accuracy and consistency of some of those results.

We have decided that we are going to establish a reference lab at our Kansas City facility. We are in the process of doing that right now. We hope to have that operational—our plans are to have it operational before the next corn and soybean crop. So we hope to have it operational in July-August time frame.

The idea there is to be able to verify and validate the testing technologies that are being used in the commercial market right now to distinguish conventional from biotech crops.

That is our initial phase. We are working very closely with the life science companies. We actually have a workshop February 24 in Kansas City where we have folks from Europe coming over, as well as all the life science companies and the producer groups, to talk about how we will go about actually verifying the performance of these technologies and how best that we do it so that there is confidence in that lab.

Senator FITZGERALD. Thank you.

Thank you, Mr. Chairman.

[The prepared statement of Senator Fitzgerald can be found in the appendix on page 92.]

The CHAIRMAN. Thank you very much, Senator Fitzgerald.

Let me just follow up quickly on that. Does GIPSA have enough authority to handle the standards problems here? You may and you are obviously heading into laboratories that are very constructive but as we are thinking through the authority problem and authorization, is this a new ball game and is there some additional authority that is required? Does anybody have a feeling about that?

Mr. SHIPMAN. We currently have the authority to do what we believe is necessary at this time. One of the biggest challenges we see facing us is that through biotechnology, you are going to see so many more crops with high value attributes and we need to be ready to prepare and provide the testing and standardization for those new attributes, so when farmers bring them to market, they can have true transparent value assessed on that.

So yes, we have the current authority to carry out what we think is needed.

The CHAIRMAN. Is there some likewise cooperation, say with the Food and Drug Administration and maybe others? For example, claims are going to be made that certain products have Vitamin A or Vitamin C or various other vitamins. In other words, up to this point, as we have heard in testimony, we have been looking at it from the producer's standpoint, whether the genetic change killed the weeds and not the corn. But now, in a confirmative way, a consumer product offensive is moving that way.

Now obviously your tests are not in that area, I suspect, as to the efficacy of whether the claims are true or whether the genetic change led to the additional nutrients, for example, but how does this work with what you are taking a look at in your laboratories, as opposed to what FDA or someone else may day?

Mr. SHIPMAN. We have not been talking directly with FDA on that, where that goes, but in terms of whether it is a certain type of oil product, oil constituent within the soybeans, or whether it is the Vitamin A in the rice or something of that nature, we do expect to be moving down the road where we would be able to identify whether that particular attribute exists in the product.

The CHAIRMAN. You would be able to do that?

Mr. SHIPMAN. Yes.

The CHAIRMAN. I see. Well, that is very important.

Mr. DUNN. Mr. Chairman, I think in the future the nutriceutical and pharmaceutical properties of these events that take place are going to become more and more important. As you are aware, the Secretary is just in the process of naming an advisory committee, Biotech Advisory Committee, to assist him to look at all of these questions and try to crystal ball-gaze a little bit to see what is coming down the road and how do we have prepare for that for the future because frankly, we are not there yet.

The CHAIRMAN. No, and we are being overwhelmed. The war is on and we are just gearing up for it. So I stress the urgency and applaud what the Secretary is doing.

Senator Conrad?

STATEMENT OF HON. KENT CONRAD, A U.S. SENATOR FROM NORTH DAKOTA

Senator CONRAD. Thank you, Mr. Chairman, and thank you for having this hearing and thanks to the witnesses.

Sunday afternoon I was in Manville, North Dakota for a meeting with farm families and I think it is fair to describe them as dispirited, disheartened, very anxious about what the future holds, and wondering when there is going to be a response to change long-term farm policy because I can tell you, they believe that this policy is not working.

We continue to be hit by what I call the triple whammy of bad prices, bad weather and bad policy. We cannot do much about the weather but we can sure do something about the policy.

I notice this morning, Chairman Lugar, that you urged President Clinton to push Europe on agricultural products in the National Journal's Congress Daily and that you had mentioned my bill and indicated that I had introduced a bill to require the United States to match EU agricultural export subsidies. It says here "Lugar said he thinks the issue of U.S.–European agricultural relations should

be dealt with 'more in terms of NATO.'" I think that is pretty close to an endorsement of my bill.

The CHAIRMAN. Not necessarily. That may be a little bit of a stretch.

Senator CONRAD. That is the way I read it.

Senator ROBERTS. Senator, does that mean we bomb Brussels?

Senator CONRAD. I do not know exactly what Senator Lugar had in mind.

The CHAIRMAN. We'll have another hearing on that.

Senator CONRAD. I tell you, my own conclusion, after being in Seattle, is that it is very clear to me we have to have leverage to be successful in negotiations. We do not have any leverage with our current farm program.

I asked this group yesterday if the Russians had fifty-thousand tanks and we had ten-thousand tanks, would the first move of the United States Congress be to cut our tanks in half? Would we go to five-thousand tanks? Because that is exactly what we did in agriculture policy in the last farm bill. They are spending $50 billion a year to support their producers; we are spending $10 billion. And under that budget part of the farm bill, we cut our support in half on the interesting notion that if we just set a good example, the Europeans would follow suit.

Well, they have not followed suit. They are not going to follow suit. And I believe it is time for a vigorous response by the United States. I think we have to rearm if we expect to be successful.

So I wanted to say that to you and this whole question that is before us in this hearing on concentration is very much on the minds of the people that I represent in this meeting yesterday.

We have talked before about concentration in the livestock sector, that under the HHI index, which rates concentration, in livestock in 1996, the last year that we have full figures, was one-thousand-nine-hundred-thirty-five on the HHI index and eighteen-thousand is highly concentrated. So we see very serious concentration in the livestock industry.

But we do not only see it in livestock. We also see it in grains, and I want to just bring to the attention of my colleagues this chart that looks at flour milling. This goes from 1973 to 1990 and you can see the red represents the four largest companies and their share. We have gone from the four companies, the four largest companies controlling 33-percent of the market to 58-percent in 1998, and that is doing nothing but increase.

On this note I would like to say that from the viewpoint of agricultural producers, we are talking about the problem of monopsony, in which there are few buyers, rather than monopolies, in which there are few sellers, and we see a very clear and disturbing example of monopsony power in the grain industry from the testimony of the chief economist of USDA last year. And this chart shows what he reported to us, that farm exports controlled by four firms—we see in corn, 70-percent is controlled by the top four; in soybeans, 62-percent; in wheat, 47-percent.

And control of regional export markets is even more concentrated, with these same four firms controlling 100-percent of some commodities through specific ports. In the case of wheat, the

level is 86-percent through the Pacific Northwest and 81-percent through the Great Lakes.

That leads me to my question very quickly. My understanding is that the Secretary, the mandate in this area can be interpreted as proactive, even preemptive, that the USDA has the power to intercede before damage occurs. I would be interested if you agree with that interpretation and second, if you do, if you could describe for the Committee any recent examples of this type of proactive and preemptive action on the part of the Secretary and USDA.

Mr. BAKER. I am not aware of that with the P&S Act. We have to prove—we have to have the fact that a harm was committed before we can take action. Now we guard against it and all but as far as taking an action ahead of time, I am not aware of that.

Mr. DUNN. Senator, I think as you read Section 202 of Packers and Stockyards, it does allude to any potential problems. However, there has not been any case built up over the years, the 75-years plus of this Act, where USDA has gone to court and said, "We are going to take that proactive strike."

And, as a result of that, it is extremely difficult—it is impossible for us to be able to go in and make a case that we are going to do this because we think this is going to happen and we think that this is going to be the result. There is no case study to be built upon there.

In fact, we have had rulings from the court saying that we have to show causality on things.

Let me just say that as I read the language, it does have a broad mandate to the Secretary to take action. And I can understand when it has not been done before, but I will tell you, as I look at the concentration that is occurring, it is very clear to me that harmful effects flow from this kind of concentration, that when you have many sellers and few buyers, the ability to affect markets grows exponentially with greater and greater concentration.

And I would just say I hope it is communicated back to the Secretary that I think you have a situation in which we ought to test the envelope. We ought to go out there and take preemptive action and let courts wrestle with this question as to whether or not there has been this kind of grant of authority by the Congress of the United States through the Secretary.

Obviously you would want to have very carefully made the case that there is danger developing and that is occurring, but I really think the Secretary, and I know that you do not have precedent for this, but that the Secretary has substantial authority here that has not been exercised.

The CHAIRMAN. Thank you very much, Senator Conrad.

Senator Roberts, I understand you have a couple of questions.

Senator ROBERTS. Yes. And if these questions have been asked before, I apologize. I was late for the hearing.

Mike, can you tell me? We had an 18-month moratorium amendment introduced by Senator Wellstone in this session, or in the last session. Did the administration take a position on that?

Mr. DUNN. No, we did not take a position. I do not believe we were asked to.

Senator ROBERTS. Does the administration have a position on a moratorium of that nature?

Mr. DUNN. Not at this time.

Senator ROBERTS. Do you plan to have one?

Mr. DUNN. If we are requested, we will.

Senator ROBERTS. Why don't you do that? I am not sure that I have the authority to request it but I think it would be helpful. That amendment was defeated by a large margin but did not—I do not mean to portend that, that would be the case if people could be convinced that we would have the answer to the problem. That is what I am saying.

What about the administration's position?

Senator Daschle has a packer ownership bill and we have several bills introduced on both sides of the aisle in regard to packer ownership. Has the administration taken a position on that?

Mr. DUNN. Not at this time. We have not.

Senator ROBERTS. I think that would be helpful if you could address—I am not saying you have to address that specific bill but at least I think generically it would be helpful.

Are you thinking of proposing legislation in regard to mergers and ownership from the standpoint of the administration, so we would have something to work with, as well as some funding?

Mr. DUNN. That would be something that would come under the jurisdiction of Justice. We would have to consult with them on that.

Senator ROBERTS. And then with Doug, you are going to be doing that?

Mr. DUNN. That is correct.

Senator ROBERTS. OK, thank you, Mr. Chairman.

The CHAIRMAN. Let me just underline and ask on behalf of the Committee, Secretary Dunn, that the administration give us a formal viewpoint on Senator Wellstone's legislation and on Senator Daschle's legislation. These are both fairly well known legislative vehicles and they have been mentioned in our hearing this morning and it would be very helpful to have informed comment from the administration on both of those bills.

I thank all three of you for helping us this morning, coming in with your testimony and your responses.

The CHAIRMAN. At this point I would like to call upon our next panel to come to the desk. That would include Dr. Philip Paarlberg of Purdue University, West Lafayette, and Dr. Kenneth Foster of Purdue University, West Lafayette, Indiana.

Would the Committee come to order so that we will all be able to hear clearly the next witnesses?

Dr. PAARLBERG AND DR. Foster, it is a personal privilege to have both of you here. You know of my admiration for your work. We have cited it on other occasions prior to today. We are looking forward to hearing from you directly. Please proceed.

STATEMENT OF PHILIP PAARLBERG, PURDUE UNIVERSITY, WEST LAFAYETTE, INDIANA

Dr. PAARLBERG. Thank you, Senator Lugar, members of the Committee. I would like to report with Dr. Foster, my colleague, on the results of the staff paper done at Purdue University by a number of us and I will report on the part that I did and Dr. Foster will cover his area.

We have already heard this morning about the level of concentration in the industry, so I will not go back through that material. You have heard the numbers. We mentioned the Herfindahl Index. One of the advantages of a Herfindahl Index is that it can be used to estimate the number of symmetric firms in an industry, and what I mean by that is if all the firms are the same size, how many would there be in that industry?

In the case of the hog slaughter industry, the symmetric firm number for 1985 would be twenty-two, which is sufficiently large to avoid distortions in pricing. By 1997, the last data that I have for the hog packing industry, that had fallen to ten. Now, there is no specific value with this index that says okay, now we have serious pricing problems, but once an industry gets down to about ten, you begin to become concerned.

So what we did is we tried to construct a model that would illustrate how concentration might affect the hog price as the number of packing firms increases and decreases, starting at the base value of ten.

Now, because so much information that we needed to construct this thing accurately was not available, we made a number of assumptions. What we did is we assumed that we had identical packing firms and varied these from one to twenty. The model then calculates how the markdown or price gap from a perfectly competitive hog price changes in response to changes in firm numbers. This markdown represents the potential market power of packers to pay less for the hog input than would have been the case under perfect competition.

If there are twenty firms, which is a situation similar to the late 1980s, the price paid to producers for hogs is 95-percent of the perfectly competitive level. As the number of packers falls, the gap on the price to farmers increases. At first that gap will remain small. Starting from twenty firms, this firm number does not initially lead to much larger markdowns. When you start at twenty and go to fourteen instead, then the hog price is 90-percent of the competitive level, instead of ninety-five at twenty.

When you go from fourteen to eight firms, the markdown goes from 10-percent to 18-percent. Once the firm numbers drop below about 5 in this type of model, the markdown increases sharply.

Now, as I said, the 1997 Herfindahl Index indicates an industry of about 10 symmetric firms. The illustrative results show that in a range of 8 to 10 equal sized firms, a critical transition between the magnitude of the markdowns occurs. Below 8 firms, the markdowns accelerate. Above 10 firms, the change in firm numbers does not really affect the markdown very much.

In the case of the model used here, if the industry is presently at eight to 10 firms, a policy designed to increase firm numbers may be less critical than a policy designed to maintain firm numbers. In other words, it may be the concentration which has already occurred has not pushed us very far below the competitive price, but further concentration could have serious adverse consequences for producers.

Now, one of the things that you need in this is to know the precise shape and location of this relationship. Unfortunately, the one we have can only serve as an illustration because critical pieces of

the puzzle are missing. We made assumptions which may incompletely reflect the hog and pork sector, and these pieces have to be inserted into the analysis to accurately analyze the consequences of increased or decreased packer concentration. With additional data, it will be possible to narrow the uncertainty of what is occurring and providing that analysis should be a high priority.

In summary, we are witnessing the industrialization of agriculture. These structural changes have been pronounced in the pork sector and raise important questions about the competitiveness of both the product and input markets.

There is evidence of increased concentration to the point where public vigilance is warranted. Concentration indexes are high and may be reaching a point where markdown pricing on hogs could be significant. It is important for us to have the required information to do this analysis as soon as possible to properly assess where we are in this respect. Thank you.

[The prepared statement of Dr. Paarlberg can be found in the appendix on page 94.]

The CHAIRMAN. Thank you very much, Dr. Paarlberg.

Dr. Foster?

STATEMENT OF KENNETH FOSTER, PURDUE UNIVERSITY, WEST LAFAYETTE, INDIANA

Dr. FOSTER. Chairman Lugar and members of the Committee, Dr. Paarlberg has shown that greater consolidation in the meatpacking industry could lead to lower live animal prices paid to farmers. Likewise, increased captured supplies, via vertical integration and/or contracting, have the potential to lower prices on average and increase the variability of prices.

This is especially true for those producers who are not a part of the captured supply chain.

Packers are motivated to coordinate their supply of live animals by the large fixed costs associated with slaughter plants and the large transactions cost of purchasing large numbers of animals on a daily basis. In order to reduce their cost per unit of wholesale meat, packers need to slaughter as many animals as possible. For modern plants, this means thousands of animals each day. The risk of coming up short motivates the use of company-owned animals and contracted purchases to ensure that the appropriate quantity and quality of animals arrive as needed. With captured supplies, transaction costs are also reduced by not having to haggle over the price of each individual load of animals.

Logically, packers attempt to capture the highest quality animals via contracts and vertical integration. This leaves the lower-quality animals to establish prices in the open market. Because payment schemes for most of the packer contracted animals are based either on a market price, a spot market price, or the Chicago Mercantile Futures price, substantial vertical coordination may create a downward bias in the prices received by many livestock producers.

Mitigating these downward biases in live animal prices will not be an easy task. The strongest public policy instrument is antitrust. Clearly, breaking up the larger packers would help mitigate markdown pricing due to concentration if it exists. However, sound economic rationale, unassociated with market power, could be moti-

vating contracting, vertical integration, and concentration. If the societal benefits of these rationale exceed the costs of markdown pricing, then the antitrust approach would not be justified.

It is my opinion that alternative public policies do exist that could offset the price impacts of these business structures without completely foregoing their benefits. The focus of these policies would be on increasing the bargaining power of pork producers. Unfortunately, the livestock producing community has little experience and expertise in using these alternatives and will likely need public policies and assistance to get them functioning.

Cooperative production and marketing appear to be possible ways to offset the impacts of consolidation and integration in today's pork industry. Any strategy that places livestock producers in a more symmetric bargaining position with packers will make it more difficult for packers to exploit prices or contract terms. It should be also more difficult for a packer to terminate a contract or to force less favorable terms on the producer community. The packer, in need of animals to fill a daily kill, will be compelled to negotiate a more competitive price if producer power is increased.

A competitive cooperative scheme would require a sizable network of today's large, independent producers. Forming such networks or cooperatives must be nurtured by public policy. Our research at Purdue has demonstrated that there are a variety of ways to structure these entities that may also allow the producers to capture cost reductions and gain access to new and possibly proprietary technologies.

Tax incentives or deductions for members of these production and marketing networks could provide incentives not only for producers to enter such arrangements, but such policies could also be fashioned to provide disincentives for producers to break away from the group in an effort to capture short-term gains. Current exemption from antitrust constraints provides some benefit for cooperative formation. However, undercapitalization is the most common cause of failure among new cooperative ventures.

The approach needed by such groups is fundamentally different from the traditional livestock marketing cooperatives of the past. In the past, farmers independently produced the animal type of their choice and marketed them on the day of their choice to various markets.

If the cooperative alliances of the future are to increase the bargaining power of producers, then the production systems of the cooperating farmers must be coordinated. Coordinated production will allow the group to provide a steady supply of hogs of a uniform quality to a single packer. This supply chain must be closely managed to deliver a large number of animals on a daily basis because fluctuation in supply is not attractive to packers and reduces producer leverage.

Marketing orders provide another possible avenue. I will not go into great detail about those. In my written testimony there is some more detail. Marketing orders have been used in several agricultural commodities where producer bargaining power is or has been a concern.

In summary, two major policy options are antitrust activity on the one hand and nurturing increased market power of pork pro-

ducers on the other hand. With current knowledge, we cannot recommend breaking up existing packer concentration. Such actions can be extremely contentious and may be contrary to society's best interest. However, public policy can assist producers in gaining countervailing market power.

Finally, caution should be exercised against blanket condemnation of strategies adopted by packers or producers that enable them to compete successfully in an increasingly international marketplace.

I would like to thank the Chairman and the Committee for inviting us here to give our opinion.

[The prepared statement of Dr. Foster can be found in the appendix on page 99.]

The CHAIRMAN. Well, we thank both of you for your paper and for your testimony.

First of all, Dr. Paarlberg, in the model you have established, you pointed out that you had a lot of data, but some information was not available to you. Is this still a work in process? In other words, as you take a look at this concentration, what you are saying is very specific, as I understand it. If you get to fourteen symmetric firms, the producer might get 90-percent of the price that he would have gotten in the old days when you had a whole galaxy of them.

So already you have some reduction of the prospect for producers, even at the level of fourteen, but now you are pointing out that we have progressed to a level roughly of 10 on your model, which is above 8, where the discount is 18-percent and falls abruptly after that. But, of course, although it is lower than ninety, somewhere between an eighty-two and a 90-percent of the regular price or what it used to be may be a 10 to 15-percent discount or so already.

This is the first time that I have heard theoretical economics try to quantify this. In other words, in the past, people have come to our Committee and they talk justifiably about the hurt that is involved, but the ability to put a percentage on it and to identify this with a specific amount of concentration is quite a contribution. This is why I am wondering whether your model continues to grow with more nourishment of fact and data or how would you describe this process?

Dr. PAARLBERG. This was just an early, a first, quick pass at the question. What we have done now is to go back and do a number of things. One is we have tried to—this held the price of pork constant. So it implicitly assumed there was no cost to consumers one way or the other. So we have now introduced some price responsiveness.

We have tried to look at the economies of scale question. Someone says you know, you could benefit because as these packers get large, they are able to drive unit costs down, so that could be a positive sign, and we are attempting to integrate that into the process.

This simple little model did not look at the contracting issue, vertical linkages, so consequently, we have tried to introduce to markets two types of hogs. Basically, one would be an integrated hog, coordinated hog, and one would be an independent. We are also

trying to do this over time and look at a sequence of twenty quarters and how the model evolves.

So it is an ongoing process and at this point it just needs more validation to make sure that it is reasonable.

But again what I find is we do not really know a whole lot about economies of scale for the packing industry. We suspect they are there, but we do not have a lot of hard information. The computer requires a number, so that is where we are going with this.

The CHAIRMAN. Will you be making periodic reports to the rest of the world to bring us up to speed?

Dr. PAARLBERG. I think our department has that plan, yes.

The CHAIRMAN. Great. Well now, you have demonstrated, even if inexactly, that concentration probably has an effect upon producers. As you say, in one new recent part of the model, you hold the consumer situation constant.

Dr. PAARLBERG. Right.

The CHAIRMAN. So that implies that you are now talking about how the pie is divided between, say, the packers and the hog farmer out there if the consumer is sort of held harmless in this process and you are finding that the returns for the producer are lower.

Dr. PAARLBERG. Yes.

The CHAIRMAN. Now then the question that Dr. Foster addresses—well, both of you do in your paper—is what do you do about it? You know, the data that you are presenting are very important so that this idea of unintended consequences does not jeopardize the exercise. This is why, as I gather, you say if you come to a certain point, antitrust may not be the best tool. You do not rule it out but given the level of concentration in the hog industry, at least, it may be more of a bargaining position by these producers if they could cooperate with each other.

And, as you have pointed out in your paper, in the past they have not cooperated all that well, so you are suggesting maybe public policy, tax incentives to get people together, or even disincentives if they fall apart, which is another question altogether, I suspect. But if they do get together, then somehow they enter into this arena of bargaining with the packers and they do better on behalf of hog farmers generally because they have that much control over supply and so forth.

What sort of reaction have you had from hog farmers to that? Have you tested this out with people who are in the field and what do they think about it? Do they want to cooperate? Do they understand why they might be advantaged by doing that? What sort of feedback do you have?

Dr. FOSTER. I guess that is pretty much directed at myself. Frankly, my interest in this arose from the pork producers, not from myself. I was motivated by individuals calling me, requesting what sort of information that Purdue University or the land grant universities might have about developing cooperative structures for production systems and marketing.

We got involved in this originally a number of years ago when we were examining the effects of various new technologies that were arising in the pork industry and looking at efforts for small, independent farms to gain access to those technologies from the production point of view.

That work we have finished. It sat on the shelf for a number of years and a year ago or so when prices became so low, the interested farmers and this sort of thing, from a marketing perspective, started to creep back up, so we began to get interest.

I have worked with two different groups of producers in Indiana. We are already forming cooperatives or limited liability corporations for group marketing and they seem to have very strong groups, a large number of producers, what we would consider in Indiana medium to large-size operations, traditionally family farms.

So the mentality of the producer is changing a bit, or at least it was changing. Now perhaps with higher prices, the concern will go away and we will go back to the status quo. That is yet to be seen. And that is one of the concerns that we tried to address in the paper, is that there has to be some mechanism, when prices do rise and individuals might be able, for the short term, to gain higher prices marketing independently, that they do not abandon the network because the ability of the network to supply on a regular basis is the crux of the matter. If they cannot do that, then their bargaining power is limited.

The CHAIRMAN. Senator Roberts?

Senator ROBERTS. Pill, are you any relation to Don?

Dr. PAARLBERG. Yes, that is my uncle.

Senator ROBERTS. I could see some of the expertise that the family seems to have in giving us advice and counsel as we wade through all of the challenges that we have.

Well, thank you for coming and thank you, Ken, as well.

Mr. Chairman, I feel compelled to say that if Dishot Carter had not turned the wrong way, that Drew Breese would not have completed the pass on behalf of Purdue in the Alamo Bowl, but then that is past history.

Dr. PAARLBERG. It was a good game, though.

Senator ROBERTS. It was a good game. We look forward to a rematch one of these days.

I think the Chairman has indicated something very important. If you can somehow quantify the hurt or give us—I do not know if it is possible to give us a formula or a set of figures that would help trigger some alternatives, but you are certainly on the right track and I give you a lot of credit in that regard.

Let me just ask you some pointed questions. If Indiana, and I am not sure that this is the case but we have different farm groups in Kansas and, for that matter, all around the country discussing the possibility of both moratoriums on mergers and a ban on packer ownership.

What would you advise if the Indiana legislature were to suggest that or, for that matter, what would you advise the Congress? First on the moratorium, on an 18-month moratorium on mergers, what would be your response?

Dr. PAARLBERG. I think to some extent I would first want to know what we mean by the merger. There is a difference here. What we are talking about is horizontal, packers buying packers, not necessarily packers vertically integrating, because that is not in the paper.

So what I would say is our work is suggesting that you are at a critical point here where if you go down and have fewer and

fewer firms, fewer and fewer packers, that markdown is going to increase and it is going to do so at an increasing rate.

So what we are saying in the paper is we think it is prudent to evaluate where we are on holding the line at existing numbers.

Dr. FOSTER. Can I just interject?

Senator ROBERTS. You certainly can.

Dr. FOSTER. From the point of view of Indiana, we just finished a statewide committee that looked into contracting issues for the state. Basically our recommendation was for continued diligence and education.

I think what we discovered was that anything that was done on a state level could only harm our industry for the state, and experience in other states has borne that out. South Dakota implemented a mandatory price reporting act. The day after that went into effect, essentially the spot market for cattle in the State of South Dakota disappeared because it required things like objective pricing mechanisms.

So the individual who came to a fellow's farm and evaluated on visual appraisal the quality of a set of cattle and quoted a price, that was no longer allowed. So at that point, individuals had to load their animals up on trucks, haul them to market with basically no price discovery.

Senator ROBERTS. I think that is extremely important, Mr. Chairman.

You mentioned tax incentives. I will find the paragraph here. "Tax incentives or deductions for members of production and marketing networks, corporations, cooperatives and alliances could provide incentives not only for producers to enter such arrangements, but such policies could also be fashioned to provide disincentives for producers to break away from the group in an effort to capture short-term gains as a "free rider," etc., etc.."

We have an outfit in Kansas called U.S. Premium Beef. Your comments in regard to group marketing I think were especially pertinent.

I am not sure if I understand how these tax incentives would work. I am not asking for a complete report here but could you sort of help me out in this regard?

Dr. FOSTER. I am not sure I know exactly how they would work either, Senator, but what we do know is that undercapitalization is a primary problem that faces cooperatives approaches.

Senator ROBERTS. That is the key that I was getting at. But you say that we should be considering some form of tax incentives to answer that kind of a serious problem?

Dr. FOSTER. Ideally, that capitalization would come from producers. We might consider outside investors but after the past 24-months in the hog industry, there are not many outside investors interested in investing there.

So we have to do something to encourage—if, in fact, this is the solution, somehow we have to encourage a large number of members because we are talking about huge numbers of animals really to be able to affect any sort of symmetric bargaining power for producers. And to get those large numbers of individuals to align with one another and stay aligned, it will probably take some sort of economic incentive up front.

Senator ROBERTS. The other thing that you suggested was marketing orders, and I must say, Mr. Chairman, these are some innovative suggestions, as opposed to the ban on mergers and the ban on owning livestock.

You say marketing orders are used in several agriculture markets where lack of producer bargaining power is a concern. We are all familiar with out West in regard to the fruits and the vegetables and, more especially, with dairy. I am not too sure I want to go down that road in regard to following the example of dairy.

Dr. FOSTER. I am not sure that I would, either. And realize that when we put this paper together, we were trying to cover the bases of policy alternatives, and that is why I think if you read the paper, substantially less time and space is devoted to marketing orders.

Clearly there are some serious problems with marketing orders——

Senator ROBERTS. Yes, there are 11 lines here. There are a number of lines more in your other suggestions.

Dr. FOSTER. That's right.

Also realize that the Ag Marketing Act that allows for marketing orders does not include pork, so it would take some significant legislation——

Senator ROBERTS. Mr. Chairman, my time has expired. I really want to thank these witnesses for maybe getting us beyond some of the easier things to say in regard to this issue. And the thing that I would like to underscore in regard to Ken's testimony is he says, "However, public policy can assist the producer in gaining countervailing market power," and that is a whole area that I think we should explore as best we can and I thank the witnesses.

The CHAIRMAN. Well, I agree with the senator and that is why I have encouraged updates as the model rolls on because more data, more information may be available to us.

Senator Fitzgerald?

Senator FITZGERALD. Thank you, Mr. Chairman.

Dr. Foster, I was intrigued by what you said about encouraging cooperatives, too, and I did want to follow up with some of the questions Senator Roberts had. You said that undercapitalization is the biggest problem for new coops.

Were you thinking when you mentioned the possibility of tax incentives to encourage the participation in coops, were you thinking perhaps of somehow providing a tax deduction for the capital contribution?

Dr. FOSTER. Ideally, some sort of tax deduction or credit, yes, for these individuals. We really had not thought that through in any sort of detail, but some sort of economic incentive.

Senator FITZGERALD. It seems to me that there must be some barrier that farmers are deterred by the large capital contribution they have to make to join the coop, to buy their membership in the coop. They may make it up in a few years but it is that up-front cost that is deterring them.

Are there studies that show that after they are members of the coop, that they are liable to do better, to get better prices and to retain more of the value at their farm level?

Dr. FOSTER. I am not aware of any specific studies, but I think in terms of individuals' willingness to invest in these ventures,

there is a fair amount of uncertainty in terms of the success of those ventures. So it becomes a capital investment decision under uncertainty, which gets us into the issue that we do have the option to wait and invest later, and that option becomes quite valuable when there is significant uncertainty.

So I think basically we could price the option to invest in the coop and that would give us some idea of what sort of tax incentive would be required to get the typical individual to do that.

Senator FITZGERALD. What about the potential for maybe a loan program to help people make their capital contribution to a coop? Are there any such loan programs available now?

Dr. FOSTER. I would have to defer to the people from the Department of Agriculture.

Senator FITZGERALD. It was mentioned earlier, the Cooperative Extension Service that the previous panel mentioned. What role do you think that Cooperative Extension Service could play in providing technical assistance to farmers who are involved in cooperatives?

Dr. FOSTER. Let me clarify. I think what the previous witnesses were referring to was the Coop Service within USDA, not the Cooperative Extension Service. So let me address both of those because I think both play a role.

Senator FITZGERALD. OK.

Dr. FOSTER. The Coop Service at USDA currently is funding a cooperative agreement with myself and Dr. Joan Fulton at Purdue to do research on the effectiveness or potential effectiveness of pork producer coops, both from the production and the marketing perspective. So I think that they have a role in regard to funding research.

They have some excellent people in the field. I was at a meeting with one of the groups that I have been working with in Indiana and one of the field staff from USDA Coop Service was at that meeting he is anincredibly skilled, experience individual with a lot of potential to provide assistance, technical assistance to people who are developing cooperatives.

Not all of those groups are interested in developing as cooperatives and I am not sure when we go beyond that business structure that the Government provides sufficient assistance.

The Cooperative Extension Service, of course, is there but extremely overworked at the local level, so whether or not they have the individual time to devote to this, I have my doubts.

Senator FITZGERALD. You are already researching this area. Have you come across any statistics on what percentage of, say, livestock producers would be involved in coops nationwide?

Dr. FOSTER. I do not have those statistics with me. Of course, it varies greatly by industry. If you went to the dairy industry, it is much higher.

Senator FITZGERALD. Eighty-four, 85-percent.

Dr. FOSTER. That is right. And if you go to the pork or beef industry, it is very near zero.

Senator FITZGERALD. Well, what has encouraged the formation of the cooperatives in the dairy industry?

Dr. FOSTER. Well, quite a bit of it was favored by the marketing order.

Senator FITZGERALD. Back in the 1930s.

Dr. FOSTER. Yes.

Senator FITZGERALD. OK. Well, that is very interesting.

And I am going to have another commitment shortly and Mr. Chairman, I just wanted to welcome, at this opportunity, to welcome a couple of my constituents who are going to be on subsequent panels.

The CHAIRMAN. Great.

Senator FITZGERALD. Ron Warfield, the president and recently reelected president of the Illinois Farm Bureau from Gibson City, Illinois is here. And on the panel after him, on the fourth panel, Mike Clark from the National Corn Growers Association. Mike, welcome. Mike is from Homer, Illinois and also involved with the American Soybean Association, as well as the National Association of Wheat Growers. Is that correct? All those organizations. I want to welcome you here to Washington. Thank you for coming.

And thank you to the panel here. Thank you.

The CHAIRMAN. Well, thank you very much, Senator Fitzgerald. Let me mention that supporting the Purdue professors here today are Mayor Bill Graham from Scottsburg, Indiana, who is here, and out in the audience, Mr. and Mrs. Robert Fear of Montpelier. We appreciate their coming very much. Let me thank both of you.

And welcome, then, our third panel. Senator Fitzgerald has mentioned we will be hearing additional witnesses and that moment has come. Those witnesses include Mr. John McNutt, president of the National Pork Producers Council from Iowa City, Iowa; Mrs. Rita Sharma, National Cattlemen's Beef Association from Williamsport, Indiana; Mr. William Roenigk, Senior Vice President of the National Chicken Council of Washington, D.C.; Mr. Ron Warfield, President of the Illinois Farm Bureau, representing the American Farm Bureau Federation, from Gibson City, Illinois; Mr. Michael Stumo, Organization for Competitive Markets, Winsted, Connecticut; and Mr. John Crabtree, Center for Rural Affairs, Walthill, Nebraska.

I will ask each of you to limit your testimony to 5 minutes, if that is possible, and the Committee will then conduct a round of questioning following the presentations of the panel.

I will call upon you in the order I introduced you, which, first of all, would be Mr. McNutt. And Mr. McNutt, Senator Grassley has been called to the floor to manage the Bankruptcy Bill and before he left, he asked me to greet you, which I will do. It is good to have you again. You are a regular here in our Committee and we appreciate your lead-off today. If you would testify, we would appreciate it.

STATEMENT OF JOHN McNUTT, PRESIDENT, NATIONAL PORK PRODUCERS COUNCIL, IOWA CITY, IOWA

Mr. MCNUTT. Thank you, Chairman Lugar.

As you said, my name is John McNutt. I am president of the National Pork Producers Council. I am a pork producer from Iowa City, Iowa.

Let me be perfectly clear that America's pork producers expect nothing less than a fair, transparent and competitive marketplace.

Nothing less will suffice to provide us and those who follow an opportunity to earn a livelihood.

For pork producers, GIPSA is the only policeman on the beat and we are determined to give this policeman the resources it needs. We would not be here today if there were not some who have strong sentiments that GIPSA has not met all of its responsibilities.

The pork industry is changing at a very accelerated pace. These changes raise some serious questions about the effectiveness and efficiency of price discovery and the potential for manipulation of markets.

NPPC is dedicated to enhancing market competitiveness for pork producers. In the past few years we have launched a number of new initiatives toward this goal. They include the passage of the Mandatory Livestock Price Reporting Act. We got that legislation and we have to make sure it is funded sufficiently so it can get its job done.

I have named a Price Discovery Task Force that is surfacing issues of concern for pork producers and possible solutions. One of those solutions is what we call negotiating report, producers reporting prices to the Agricultural Marketing Service [AMS] so that they get part of the mix.

We also have the publication of a guide to marketing contracts to help producers in the negotiation between producers and packers, and I would like to submit that for the record.

And we have created, following some conversations here, a new producer-owned cooperative called Pork America, which has been incorporated here in January. It is designed to give producers a tool to change their position in the marketplace.

NPPC realizes that guaranteeing U.S. agricultural markets are competitive and fair is a huge challenge. We believe the attention of both Congress and the administration should focus on four general areas.

GIPSA and the USDA must do a better job of educating the public about the provisions of the Packers and Stockyards Act and what it empowers GIPSA to do. Furthermore, they must help delineate GIPSA's market and regulatory responsibility from the market concentration responsibility of the Department of Justice.

Also, the Federal Government must develop a comprehensive strategy to address the problems of agricultural markets in general and livestock markets in particular.

Today's hog market is enormously complex and technical. Information and data that were once easily gathered is now proprietary and frequently only available upon subpoena. Many hogs are priced beyond the scope of negotiation through contractual relationships whose effect on the entire market is not very well understood. GIPSA must be able to recruit, train and retain people with specialized skills. Given this job market that we are currently in, this is becoming more and more difficult. We urge Congress to help GIPSA overcome this problem immediately and give GIPSA's management the flexibility it needs to hire the best people.

Remember GIPSA must simultaneously reassure producers and deter potential opportunists. GIPSA cannot have a constant presence in the field without an adequate number of personnel.

The analytical tools and economic theories being used today, many were developed more than 50-years ago and yet the industries which GIPSA and DOJ regulate have changed dramatically. Do the four-firm and eight-firm concentration ratios and the Herfindahl-Hirschman Index mean the same things that they used to mean? The future of thousands of pork producers could hinge upon those answers, yet very little research is ongoing in that area.

We believe a competitive grants and research fellowship program in industrial organization and antitrust economics would serve a multitude of purposes and should be established now. We also need specific research to determine relevant markets for hogs, determine the effect of contract hogs and other captive supplies and estimate the impact of vertical acquisitions.

Also, ongoing research and investigative results should be delivered in a much more timely manner than in the past. Past delays of GIPSA investigations and reports have clouded the results and invited criticism.

There appear to be several areas in which GIPSA and DOJ have insufficient authority or which current law is unclear. One example is the focus of antitrust legislation on monopoly power by sellers and its relative silence regarding monopsony power by buyers. Aren't there some specific requirements which GIPSA can employ to clearly delineate what packers must and must not do on subjects such as lean prediction equations, payment matrixes and the relationship between the two? Can't basic requirements be established to ensure that carcass information or kill sheet information is understandable and reproducible by a producer with some reasonable level of math skills?

In closing, National Pork Producers Council [NPPC] is committed to a fair, transparent and competitive marketplace. We also recognize that GIPSA must play a significant role in providing market information and oversight that pork producers need.

Mr. Chairman, thank you.

[The prepared statement of Mr. McNutt can be found in the appendix on page 104.]

The CHAIRMAN. Thank you very much, Mr. McNutt.

It is a pleasure to have Mrs. Rita Sharma here. She has been a regular attender of our Agriculture Committee meetings; likewise, a distinguished citizen of my state and we appreciate your coming today. We look forward to your testimony.

STATEMENT OF RITA SHARMA, NATIONAL CATTLEMEN'S BEEF ASSOCIATION, WILLIAMSPORT, INDIANA

Mrs. SHARMA. It is always a privilege to be in the same room with you, Sir.

We thank you, Chairman Lugar and the Committee, for holding hearings regarding oversight of the Packers and Stockyards Administration and other market regulatory issues. I am Rita Sharma, a feedstock producer from Williamsport, Indiana and a member of the National Cattlemen's Beef Association.

Factors affecting livestock prices are a puzzle to many outside our industry. Recent structural changes in the beef industry have unfortunately coincided with various international economic crises,

strengthening of the U.S. dollar, supply shifts, and weather-induced volatility in costs.

NCBA has long supported strong oversight and enforcement of existing antitrust and market protection laws. However, repeated antitrust investigation by Packers and Stockyards and the Justice Department have not uncovered broad industrywide illegal activities.

Part of the frustration in the country has been that many marketing practices and industry concentration levels that are perceived as illegal are not, in fact, illegal. National Cattlemen's Beef Association [NCBA] supports timely and complete USDA implementation of mandatory price reporting legislation initiated last session by this Committee and approved and funded by Congress. NCBA urges that USDA be involved in premerger evaluation of proposed packer mergers, in coordination with the Justice Department and supports adequate funding for these agencies to accomplish their investigative functions.

NCBA further supports a premarket system and we trust the skills of U.S. cattlemen to allow them to prosper in a relatively unregulated marketplace. We rely on Federal regulators to ensure that the marketplace is free from antitrust collusion, price-fixing and other illegal activities that interfere with competitive market signals. If allowed to work, the market will recover with a minimum of government intervention and regulatory activity. For the U.S. beef industry to be globally competitive, this is an absolute necessity.

NCBA is specific regarding emerging business relationships. NCBA does not support limitation of any method of marketing fed cattle. NCBA supports a free market system. No action should be taken to alter or halt private business arrangements among operators in the beef industry. NCBA encourages producers to take advantage of opportunities to increase profits through new marketing strategies, coordination, risk management and retained ownership.

Many producers are finding innovative ways to compete in this changing cattle industry. For instance, the Five–State Beef Initiative was formed in response to strengthen economic opportunities for Eastern corn belt by providing added value to the producer and consumer through a responsive production and marketing system. The five states involved—Illinois, Indiana, Kentucky, Michigan and Ohio—are hopeful of success. A multi-state proposal from the group is available upon request.

Funding members and current shareholders of these and many other beef marketing systems are long-term professional cattlemen proactively addressing the concerns of the beef industry through bold new marketing strategies. Their efforts are focussed on improving beef demand and producing a better beef product, marketed through their own companies.

The beef industry is in many ways a bright spot among depressed agricultural commodities. Declining numbers of calves and feeder cattle, improving beef demand after a 20-year decline, improvements in Asian financial conditions and growth of other export markets are all resulting in generally higher prices. Projections are for these conditions to continue.

In part, the beef industry has recovered from the difficult times experienced in the mid 1990s because we have never relied on government to fix industry conditions caused by market forces.

We believe in free and fair private sector market forces, not government hand-outs, to manage our industry. Cattlemen have always had the freedom to farm and the freedom to fail. The historical information may make it easier for the Committee to understand why there is a great deal of caution and reluctance by the beef industry to call for dramatic expansion of government intervention in the beef marketplace. Yet we remain committed to strong oversight and enforcement of existing laws and regulations to keep the field of play level.

Mr. Chairman, the National Cattlemen's Beef Association is not naive. Its members are fully aware of the dilemmas faced by hogs, grains and poultry. We empathize, but the National Cattlemen's Beef Association wishes to deal with these issues by participating with the Congress and their agencies in evaluating current market issues and providing input as new issues arise.

Thank you, Mr. Chairman and the Committee, for the opportunity to present this information.

[The prepared statement of Mrs. Sharma can be found in the appendix on page 111.]

The CHAIRMAN. Thank you very much, Mrs. Sharma.

Mr. Roenigk?

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

Mr. ROENIGK. Good morning and thank you, Mr. Chairman, for the opportunity to present our views on this important topic.

My name is Bill Roenigk. I am senior vice president with the National Chicken Council. We used to be called the National Broiler Council but we changed our name because chicken has taken over the world, so we want to let people know what a broiler is, so we finally have told them.

The CHAIRMAN. Good.

Mr. ROENIGK. In the interest of time, I will be very brief but I request that my written statement be entered in the record.

The CHAIRMAN. It will be placed in full.

Mr. ROENIGK. Thank you.

The National Chicken Council, as we are now called, represents companies that produce and process about 95-percent of the young meat chicken or broilers in the United States. These vertically integrated firms contract with growers to raise live birds for processing and contract with breeder farms to produce a supply of fertile eggs for hatching.

The system of production, processing and marketing is highly coordinated and operates very much in a just-in-time method. Contract growers and processors are mutually dependent upon each other. It is in neither party's interest to jeopardize the economic viability of the other party. Most growers have a relatively long and stable relationship with their processor.

With respect to one of the specific issues being addressed today, the National Chicken Council is opposed to USDA having expanded regulatory authority over poultry production because such power is

unnecessary. Adequate authority and remedies already exist. In 1987 Congress fully and carefully considered the proper scope of GIPSA's administrative enforcement authority, including civil money penalty authority, with respect to the transactions involving live poultry and poultry products. Congress at that time declined to provide such authority to GIPSA for any violations of the Packers and Stockyards Act other than those related to prompt payment and the statutory trust for live poultry dealers. The National Chicken Council is not aware of any conditions that have changed nor developments that would require Congress to reverse its decision that it made in 1987.

As I noted, GIPSA does have the authority to issue cease and desist orders, level civil penalties for violations of the Packers and Stockyards Act, protections regarding prompt payment and statutory trust. Further, GIPSA can investigate and refer to the Department of Justice for enforcement to Federal courts other violations of the Packers and Stockyards Act involving live poultry; for example, weighing practices and contract compliance.

And two, Packers and Stockyards gives the Federal Trade Commission jurisdiction over our marketing practices involving poultry products. As you can see, there exists ample oversight and authority for poultry.

One other important point that should be made is unlike the red meat industry, private actions for breach of contract under common law contract principles, as well as under statutory provisions protecting growers, are available to police the 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 very important but often overlooked in the discussion of a broader issue.

Poultry is produced, processed and marketed in a very coordinated, vertically integrated system. This business model's structure is distinctly different from the methods used in red meat. For the reasons presented here and because chicken is produced, processed and marketed in a distinctly different system and because the vertically integrated firms have successful ongoing contractual relationships with the growers, it is unnecessary to burden the poultry industry with additional government regulations.

Mr. Chairman, we appreciate the opportunity to share our views with the Committee.

[The prepared statement of Mr. Roenigk can be found in the appendix on page 116.]

The CHAIRMAN. Thank you very much, Mr. Roenigk.

Mr. Warfield?

STATEMENT OF RON WARFIELD, PRESIDENT, ILLINOIS FARM BUREAU, REPRESENTING THE AMERICAN FARM BUREAU FEDERATION, GIBSON CITY, ILLINOIS

Mr. WARFIELD. Thank you, Mr. Chairman and members of the Senate Ag Committee and thank you for holding this hearing.

My name is Ron Warfield. I am president of the Illinois Farm Bureau and member of the Executive Committee of the American Farm Bureau. I am a corn and soybean farmer in Gibson City, Illi-

nois and previously, for about 25-years, fed cattle, so I am interested in that, as well.

Today I am testifying on behalf of the American Farm Bureau Federation, which is the largest general farm organization in the U.S., representing farmers in all fifty states and Puerto Rico.

We appreciate the opportunity to testify at this hearing on concentration and consolidation in agriculture. Obviously the structure of agriculture is changing rapidly. The accelerated pace of consolidations, mergers and acquisitions is one of the most hotly debated issues among farmers across the country, and I am sure you have heard that, as well.

Today I would like to reveiw the basis for the concern farmers have over concentration and consolidation in agriculture, actions that we can take to address our concerns, and improvements to policies to assist farmers in dealing with the rapidly changing agriculture.

Farm Bureau has a long history of supporting market-oriented agriculture, but farmers and ranchers need assurance that markets are free and open, that they are competitive, that they are transparent, that they send clear price signals and they are based on good information. Particularly when I hear the last panel, good information is necessary for markets to work but good information is also necessary to know that they are free and open and how do we determine if there are really monopolistic opportunities that exist? And I think there is certainly a void in information in a lot of areas.

Are markets really working the way they are supposed to? Among farmers, the frequent perception is they are not. For instance, is there competition when mergers and acquisitions have reduced the number of companies selling production inputs, causing farmers to frequently ask are the prices they pay for these inputs based upon good competition?

Is there competition when the growing use of patents on biotech seeds means private companies own and have tight control over specific seeds?

Is there competition when railroad mergers have disrupted the orderly flow of crops to export because there are fewer cars to haul corn and soybeans across the country?

Is there competition when live hog prices fall to Depression-era levels and retail prices are not similarly reduced? Researchers find it impossible to explain the spread between live hog prices and retail pork prices over the last 3-years.

Much of farmers' concerns stem from the farm-to-retail price spread I just mentioned and other events which have transpired in the meatpacking industry. Farmers and ranchers have also questioned why some packers have purchased plants, only to seemingly shut them down.

This information is provided to paint a picture of the rapid consolidation of the ag industry. Farmers and ranchers realize that the world is changing and the market system is evolving, but that said, we must also ask, is it time for our market rules and policies to evolve, as well?

Last year Farm Bureau worked with Congress to address some of these concerns. Farm Bureau has worked diligently to seek addi-

tional appropriations for GIPSA so that it may fully enforce the Packers and Stockyards Act. Also a step in the right direction was the passage of the Mandatory Price Reporting legislation last year. This legislation is designed to provide producers more market information on livestock transactions, including contractual arrangements.

Farm Bureau has assembled an action plan designed to ensure competition in agriculture and 10 specific points of that could be taken by Congress and the administration are included in the written testimony. We would hope that members of this Committee will find that these are worthy of pursuit. We would also be interested in pursuing the private sector because we are interested in pursuing that, as well, if we would want to discuss that in the question period.

The actions suggested in our written testimony address just a few of the pieces of the concentration puzzle. Farm Bureau delegates just last month approved new policy on an expanded and more active USDA role in mergers and acquisitions. They would broaden the USDA responsibility in official consultation with the Department of Justice and should bolster farmers' confidence that a thorough review of concentration of agribusiness is taking place before it is approved.

This USDA review would take into account such factors as the effect of the acquisitions and mergers on prices paid to producers who sell to or buy from or bargain with one or more of the parties involved in the merger; the likelihood that the acquisition or merger would result in significantly increased market power for the new or surviving entity, and obviously in the pork industry, as we just heard, more concentration would be extremely detrimental; the likelihood that the acquisition or merger will increase the potential for anti-competitive or predatory conduct by the new or surviving entity; whether the acquisition or merger will adversely affect producers in a particular regional area, which could be an area as small as a single state.

We have outlined a number of requests today. We hope these comments will be viewed as an indication of the degree of thought that farmers have put forward on how concentration is impacting their farming operations. Thank you for the opportunity to testify.

[The prepared statement of Mr. Warfield can be found in the appendix on page 119.]

The CHAIRMAN. Well, thank you, Mr. Warfield. Congratulations on your reelection in Illinois and your service on the Executive Council here in Washington.

Mr. Stumo?

STATEMENT OF MICHAEL STUMO, ORGANIZATION FOR COMPETITIVE MARKETS, WINSTED, CONNECTICUT

Mr. STUMO. Thank you, Chairman Lugar and the rest of the Committee on Agriculture, Nutrition and Forestry for the opportunity to speak here today.

My name is Michael Stumo. I am general counsel for the Organization for Competitive Markets. The Organization for Competitive Markets is a multi-disciplinary group of farmers, ranchers, academic, attorneys and businessmen who focus exclusively on com-

petition policy in agriculture. I am also a hog farmer from Massachusetts and I am formerly an Iowa hog and cattle buyer and I work with farmers, also, to set up cooperatives.

I come before you today with a sense of urgency, Chairman Lugar. This is not just another farm crisis. This is the end game of independent family farm agriculture. The crux of the issue is industry structure. There are tremendous amounts of money being made in the food industry, but the farm sector, the farm production sector, does not receive that money because the oligopsonistic meatpackers and the oligopsonistic retailers have positioned themselves to capture the bulk of that profit. Thus, high packer margins, high retail food margins and the end of the family farm. This is not a future. This is very quick. Five-years, we will not have an open spot market in hogs.

Feedstuffs Magazine, the number one agribusiness weekly in the country, editorialized last September that, and I quote, "American agriculture must now quickly consolidate all farmers and livestock producers into about 50 production systems." This is not just an editorial; it reflects the long-range strategy of agribusiness. It cuts through the euphemistically rhetoric of alliances and coordinated system. It is mercantilistic win-lose. Agribusiness wins; farmers lose.

How did we get here? First in the livestock sector, meatpackers consolidated horizontally; now they are appropriating the food chain vertically. For the farm production sector, that means that IBP, ConAgra's Monford, Cargill's Excel and Smithfield Foods are soaking up the productive assets of family farmers either through contracts or outright ownership.

If packers own or control the livestock, there is no independent livestock agriculture, period. Thus we have not only the open market problems of the oligopsony on the general market level and the competition, specific competition practices; we have the closure of the market through contracting. Why is contracting bad at the macro level? Why is it not merely free enterprise working at the macro level?

First, the contracts take the production off the open market, pricing becomes secret, and the open markets wither away.

Second, packers can more consciously than ever before pick the winners and the losers. In October 1998 the buyers for Hormel and Excel were talking to veterinarians in a conference call and they were talking about the production contracts that they use. The Excel buyer—they both admitted that they pick the producers that they feel will succeed to contract with. That leaves everyone else out. The Excel buyer admitted that he had zero people, zero small producers under contract.

Third, a long-term contract fundamentally transforms a farmer from a profit center into a cost center. The producer becomes a locked-in cost from the perspective of the packer, which the packer now has not only the incentives but the control necessary to reduce that cost with unilateral will. Once under contract, the packer imposes terms and conditions which reduce producer profit and management discretion and, in some cases under some contracts, increases the producer debt to the packer. It is the company store problem.

With widespread contracting, the open market withers away and producers increasingly have no choice at the micro level but to contract, because of the open market problems.

The Packers and Stockyards Act is the strongest trade regulation statute in the country. It was designed to prevent problems in their incipiency, and this is a very important distinction, Mr. Chairman, the incipiency theory rather than the past proof of harm theory. The Office of General Counsel and Mike Dunn, as you heard today, have taken the latter position—proof of harm. Thus, we have all the Economic Research Service [ERS] studies trying to analyze whether there has been harm in the past, three, four, 5-years ago or not. They use voluntarily disclosed packer data. The packers do not disclose the stuff, if it exists, that may be incriminating. It is voluntary. And they do not use the proper models, as Mr. McNutt mentioned earlier. And Mr. Dunn and Mr. Baker fail to do anything to correct these problems. It is a legal standard problem. It is a big problem.

So the Office of General Counsel [OGC], when GIPSA comes to OGC, the Office of General Counsel, with their investigation, OGC says it is not enough. Or if private parties come, OGC says it is not enough. But they have never said what is enough.

Now, we also have to distinguish between regulation and enforcement. Regulation has the whole formal process of proving and establishing a substantial basis for whether this particular practice is an unfair trade practice under the Act. And the regulator has much more power to, in fact, define that and much more discretion to do so.

In 70- or 80-years they have failed to do it. There is nothing. Nobody knows what this thing means. They just keep saying that it is very powerful authority. They have not regulated. So then they go to enforce on a case-by-case basis. They are another plaintiff in Federal court. They are trying to create meaning out of the law and then the defendants are defending with much more resources, much more expertise than OGC has, and they end up with unhelpful court dicta, without the back-up of regulatory definitions of what unfair practices are in the packing industry. So there has been failure on that end of it. And the current administration and past ones have done nothing to do anything about that.

So OGC's enforcement expertise—not only have they barred regulation but their enforcement expertise is lacking. They bring ERS into the picture with old data and old methodology. And then GIPSA just does not have the enforcement tradition, the professional tradition, the expertise that Justice has in going in and analyzing an industry. Justice has much more of all those factors—tradition, professionalism—to do that and I am very pessimistic that GIPSA will ever get up to that speed, and this Committee may want to seriously consider transferring anti-competitive practices authority over to Justice.

Thus, I propose and the Organization for Competitive Markets proposes a few things Congress may want to look at. Number one is making clear legislatively that incipiency theory is the proper standard to view harm rather than past proof of harm.

Second, ban packer ownership of livestock. If the packers own it, independent producers are gone, period. It is not going any further. Iowa lost one out of five hog farmers last year.

Next, open the contract packer market to the open market process, not secret negotiations, limit how much they can procure under the contracts and those contracts require to be open bidding; anybody can bid.

And lastly, enable the private sector to enforce the Act, as well, with attorneys' fees for lawyers because farmers cannot get lawyers if they want to get enforcement under the Act. They cannot afford lawyers. Attorneys' fees would go a long way.

And I apologize for going over but I appreciate the opportunity of being here, my first time ever at a hearing.

[The prepared statement of Mr. Stumo can be found in the appendix on page 127.]

The CHAIRMAN. Well, thank you very much for your analysis and for your very constructive suggestions.

Mr. Crabtree?

STATEMENT OF JOHN CRABTREE, CENTER FOR RURAL AFFAIRS, WALTHILL, NEBRASKA

Mr. CRABTREE. Mr. Chairman, senators, thank you for inviting me here today. My name is John Crabtree and I lead the Market Structure Project at the Center for Rural Affairs in Walthill, Nebraska.

In December 1998 and January 1999 prices paid to farmers for their market hogs dropped to unprecedented lows, something we all remember very well. Over the last year prices have risen to barely profitable levels and family farmers have left or been forced out of hog production in droves.

Livestock production in the Midwest and Great Plains has always been a family farm and ranch enterprise. Today we are replacing those sustainable and efficient—yes, efficient—family farms with a virtual handful of industrial, vertically integrated operations. We are only at the beginning of the economic debacle that we face if we allow family farm livestock production to become a thing of the past. In a recent Des Moines Register editorial, Chris Petersen, a pork producers from Clear Lake, Iowa and a personal friend of mine, lamented that "You'll miss us when we're gone." He was, of course, right in more ways than most of us care to imagine.

Why should we accept the destruction of family farm livestock production? Many tell us that it is inevitable. The truth is another matter. We have been told time and again that large-scale vertically integrated livestock production facilities can do a better, more efficient job of raising livestock, but research tells us a different story. Iowa State University economist Mike Duffy's research analysis of Iowa farm records demonstrates that economies of size run out at about one-hundred-fifty sows farrow-to-finish. The most efficient one-third of hog producers in the University of Nebraska Swine Records Program sold two-thousand-six-hundred-seventy-eight pigs and as pork producer friends will tell you, that is not a very large hog farmer anymore.

The destruction of family farm livestock production is not inevitable. It is the result of choices—policy choices, administrative

choices, and enforcement choices, choices made by people, and we can choose another path. Farmers and ranchers over the last year have fought furiously to create the kind of future in livestock production that they want. They ask for nothing more than access to a marketplace and the chance to compete on a level playing field, something that has been consistently denied them of late.

For years, the Center for Rural Affairs, other farm organizations and the farmers and ranchers who support our work were told that mandatory price reporting legislation was out of the political reality. Then, in 1999, something rather amazing happened. Farmers and ranchers from throughout rural America started coming together to change that political reality. They found some state legislators who agreed with them and they passed price reporting legislation in five states.

And they did not stop there. They changed long and closely held positions of key commodity groups, they lobbied Congress and they kept the pressure on until mandatory price reporting had changed from the impossible to a political imperative. And then this Committee responded by working diligently to create good, sound, strong price reporting legislation, which became the law of the land. That is how things are supposed to happen in this society, thankfully.

However, the same farmers and ranchers that challenged the status quo and won note the job is not done. If we are to create a future for family farm and ranch livestock production, there are more issues that need to be addressed, that must be addressed, and two needed reforms stand out.

The first, which is the focus of my testimony today, is prohibiting price discrimination in the livestock markets. When family farmers sell hogs, they get significantly less than large-scale pork production companies just because they lack the economic power to demand volume premiums. USDA's 1996 Western Corn Belt Procurement Investigation demonstrated that prices paid to producers clearly increased with seller size. That was in 1996 when the negotiated spot market demand for hogs was about triple what it is today. Volume-based premiums are undoubtedly far more prevalent today than they were 4-years ago.

Now an effective price reporting program will provide important information for the Packers and Stockyards Administration to spot this routine price discrimination that occurs in livestock markets today. However, the information alone will not suffice.

The Packers and Stockyards Act prohibits undue price preferences and grants USDA broad authority to stop unfair trade practices in their incipiency. That authority is unused. Secretary of Agriculture Dan Glickman recently that USDA would "not allow farmers to become serfs on their own land" in reference to concerns about concentration and consolidation in the seed industry. This statement rings hollow when one considers that the Secretary and Packers and Stockyards have done little to stop the same thing from happening with pork producers in this country.

The Secretary should start to rectify this inaction by issuing administrative rules that clearly define and aggressively prohibit undue price preferences in livestock markets. The reasons for

USDA's inaction on this issue are unknown to me and that inaction is, to say the least, confounding.

I have attached to my testimony language that the Center for Rural Affairs has proposed as a starting point this afternoon. In this proposal we recognize that packers should be able to pay premiums for measurable and definable differences in carcass quality and transactional costs but that volume-based premiums that simply reward economic power over hard work and efficiency reduce competition and diminish the marketplace and should be prohibited. Every farmer that I know would be more than happy to put their hard work and skilled management up against the largest corporate hog producer in the country if they knew that they had a marketplace that would judge their livestock on a level playing field and price them accordingly.

Issuing rules on undue price preferences is not only something USDA can do but must do if they are serious about restoring competition in the livestock markets. USDA officials in the Office of General Counsel have argued to me and others that by defining undue price preferences, the authority under the Packers and Stockyards Act will be narrowed and therefore diminished. However, since that authority is virtually unused currently, what we have today is a livestock market that has essentially no rules whatsoever regarding price discrimination.

The Center for Rural Affairs sought the legal opinion of Professor Neil Harl of Iowa State University in this regard. I have attached to my testimony his letter in response and I hope that will be put into the record. In this letter Professor Harl clearly points out that USDA has not fully exercised the authority granted under the Packers and Stockyards Act to promulgate rules, especially in the area of price discrimination in livestock pricing.

USDA seems to have adopted the stance that volume premiums that reward economic power over hard work and efficiency are "the American way." But in truth, the American way has always been the belief that hard work and efficiency should be rewarded and that competition enhances the marketplace.

Finally, the second much-needed livestock market reform is a prohibition on packer ownership of livestock. Senators Grassley, Kerrey, Johnson, Senator Daschle and a number of other people have introduced legislation or will introduce legislation to ban packer ownership of livestock. I would like to take this opportunity to thank these senators and others who have voiced support for it. Clearly, the transparency that we will achieve through mandatory price reporting and a prohibition of price discrimination will not alone create a future for family farmers in livestock production if the doors to the marketplace are barred to them because meatpackers own all the livestock that they kill from birth to slaughter, as is rapidly becoming the case in the pork sector.

Legislation that prohibits or dramatically limits packer ownership of livestock is needed to keep the door to the marketplace open for family farmers and ranches.

Thank you for your time and consideration. I would be more than happy to answer any questions.

[The prepared statement of Mr. Crabtree can be found in the appendix on page 137.]

The CHAIRMAN. Let me start the questions picking up where you left off, Mr. Crabtree.

Mrs. Sharma and Mr. Roenigk, in the cattle and in the poultry industries you take the position that the packers or producers at the packer level in your industries ought not to own birds in one case or cattle in another. In other words, is the situation as you perceive it identical as that which is being described in the hog market?

Mrs. SHARMA. NCBA does not oppose captive supplies of livestock for packers. They have no prohibition against any type of ownership or any type of contractual agreement wherever it is in the cow production chain. Our belief is that part of what insulates us is our basic structure.

If you take the cow calf, the large amount of capital input, the low amount of return and the long return on capital is something that does not interest the packer. Couple that with the fact that the majority of cattle producers across the United States still are in the range of twenty, twenty-five head of brood cows. The average size brood cow herd in the State of Texas is fifteen brood cows. So we are still primarily composed of small producers who control the beginning product. The beginning product is not suited to ownership by a packer and we believe will help to insulate us from other actions.

The CHAIRMAN. How about the chicken industry?

Mr. ROENIGK. In the chicken market, the market requirements and specifications often are very, very precise. They may say 2-pounds, twelve-ounces, plus or minus two ounces. So 1-day or even a half a day on feed longer or shorter would affect that bell curve and how many would be there.

At the same time, we are seeing a growth in very specific niche markets and the barriers to entry for those companies are very small. We are talking organic, free-range, those types of chickens. And, of course, those chickens have to be very, very specifically grown to meet the market demands.

So unless you own those chickens or have a contract to produce that specific type of bird requirements, you are not going to get exactly what the market wants and therefore, you are not going to be able to participate in the market.

The CHAIRMAN. So you have contracts to specify this, essentially?

Mr. ROENIGK. Exactly, and we have in the contract rewards for doing a better job.

Mrs. SHARMA. Mr. Chairman, if I may add, the basic control we have over what type of livestock we raise is the spot market and such, as well as the packer market and what they are willing to pay for specific types of livestock. They are moving very rapidly to control the type of livestock that are raised and offered for sale by oftentimes reducing prices by 50- or 60-percent if those livestock do not meet their requirements.

The CHAIRMAN. Mr. McNutt, what is the position of the pork producers on this packer ownership of livestock?

Mr. MCNUTT. We went through an extensive process last year after delegate action to look at this whole issue and at that time, the producers decided through our Federation Council that we were not in favor of moving against packer ownership restrictions last

fall, but a lot has happened since last fall. We are listening to what our delegates have to say. We have an annual meeting coming up here in March.

Our sense, though—is as an individual producer, my sense is with what has happened to my industry, yes, it sounds like a very appealing thought to have packer ownership restriction but when I have to put the hat on that I wear here and have to look at what is the effect on the industry at large, what are those unintended consequences that are out there, are there better ways to do things to address this issue other than that very heavy hand of a complete ownership restriction? I am not very comfortable with a social control of that measure.

I think that if we are smart about looking at things that we are talking about today, fixing Packers and Stockyards, making sure that it has the authority and the responsibilities and the funding that it needs, looking for the creation and the development of new methodology for producers to empower themselves in the system through the use of cooperatives, that there might be able to be other ways to address this.

The CHAIRMAN. Well, while you have the floor, Mr. McNutt, let me just follow up because the question has been raised or at least this sort of theme floats through that these very severe conditions with regard to hog prices last year, the predictions then were that thousands of hog farmers all over the country would clearly be out of the business.

Now the census figures always follow and trail, so they are more than anecdotal but not precise. But at least as I recall, the number of hog farmers in the country is somewhere around 106,000 and perhaps five-thousand or six-thousand had been lost during the course of the year. In Indiana it was something like six-thousand-two-hundred that we used to have and six-thousand that we still have, which is still two-hundred farmers fewer, but remarkable resiliency, given the hit.

Now, what happened? Was there enough reserve or did things turn around sufficiently? Are people still hopeful? If you take a look at the time line of normal attrition of hog farmers over the course of this century, we have been losing many more than that in most years that were not visited with such a devastating price.

Mr. MCNUTT. Mr. Chairman, we have taken in excess of $4 billion out of our industry. What has probably sustained the numbers to some degree is the sense that even with that huge loss, the U.S. pork industry has still been the most profitable sector of U.S. agriculture in the last 14-years.

So bankers and so forth know that they have had a very strong track record. What it has done, though, is that now producers that are still remaining—and we have lost quite a number—their amount of options available to them are less and less. When the bank tells them, "You must contract or you don't have another line of credit," they do not have the choice that they had a few years ago when they said, "No, I want to stay on the open market."

So there has been a profound effect, even though we have not seen quite as many losses of people.

The CHAIRMAN. Let me ask briefly for Mr. Warfield, Mr. Stumo and Mr. Crabtree to add whatever they want to this dialogue and

then I will turn to my colleague Senator Roberts for his questions. Mr. Warfield?

Mr. WARFIELD. I would just comment that in Illinois, of course we do not have the up-to-date numbers but we probably did lose close to 25-percent of our producers.

The CHAIRMAN. Twenty-five percent?

Mr. WARFIELD. Yes. Now, that is based on looking at numbers. We do not have exact numbers. That is just looking at the sow numbers relative to extrapolate what happened to the numbers of producers. So we did take a significant hit and, as it was indicated, they certainly have had a lot less opportunities in terms of—and there could be some other factors——

Senator ROBERTS. Is that all producers or just hog producers?

Mr. MCNUTT. Hog producers.

The CHAIRMAN. Does it mean that farmers who had hogs as a part of their program dropped the hogs but maybe stayed with corn and beans?

Mr. MCNUTT. Yes, yes, absolutely.

The CHAIRMAN. So they are still in the market, although maybe not in the hog market.

Mr. MCNUTT. That is correct. And what we are seeing is an acceleration, a dramatic acceleration in the change that is taking place. Illinois has gone from the number two hog-producing state in the country down to number four and we have been under a very dramatic decline during this hardship time.

The CHAIRMAN. Mr. Stumo?

Mr. STUMO. Thank you, Chairman Lugar. I would like to bring your focus to the perspective of a packer buyer in a competitive market or a closed market. Imagine being a buyer that has to fill up a 10,000-head kill line every day and imagine being that buyer 20-years ago and you have to go out and compete with more firms and you have to bid openly and negotiate to fill every one of those shackles.

With the advent of concentration horizontally, you take the factor out that you are actually competing with more firms. You have less firms. In fact, I would argue that national concentration levels are irrelevant because transportation makes it unfeasible, of course, to send an Iowa pig to Washington. So I do not think we should even maybe talk about the national, look at the geographic, and that has never been done within USDA.

So we have less firms to compete against and then you take the next step of the packer owning hogs or cattle. So you see in the Northwest where there is between 60- and 80-percent captive supply and part of that is packer ownership or in other parts of the country where maybe it is thirty to fifty in beef.

So you take three-thousand to five-thousand hogs or cattle, whichever way you want to look at it; those shackles are clearly going to be filled because you have that under control. Thus, you only have to bid for maybe five-thousand to eight-thousand, but you have part of those under contract for your best guys and picked out who you think is going to succeed or who you like or for whatever reason, you have picked those. So maybe you have another three-thousand to five-thousand or three-thousand that are filled.

So you only have, say, two-thousand or three-thousand left to bid on the open market.

So number one, you have those three steps: less competition with other packers; you have locked up through packer ownership and you have locked up through contracting. Thus you only have two-thousand head to procure, going out in the market and bidding and negotiating with people every time. So those three steps.

And that is what I think this Committee maybe should look at, is how do we look at the buyer mentality here and require more competition, and part of that is to limit—to ban the packer ownership or severely reduce it. And the contracting—allow contracting and allow the benefits of contracting but open it up to bidding so there is less potential for intentional exclusion, especially of small producers or unfavored producers. And limit that security on the buyer side, not eliminate it but limit it in the interest of preserving family farm agriculture and competition. Thank you.

The CHAIRMAN. Thank you. Mr. Crabtree?

Mr. CRABTREE. Thank you, Mr. Chairman. Just a couple of things on your questions.

If my memory serves me, Iowa lost, I think, 17- or 18-percent of their pork producers last year. Nebraska, my state, about 15-percent.

The CHAIRMAN. Well, how does that reconcile with the overall figure of 5 or 6 in the Nation, with these huge losses? The counting must be very different in some areas.

Mr. CRABTREE. I think the thing that is interesting is when you look at the census, the numbers that were lost were, of course, not lost across the board but typically from the smaller producers, the numbers of smaller producers, where there still are a lot more. These are producers that simply have not had access to contracts, that bore the brunt of that $8 hog market.

The reality was when hogs were $8 on the spot market, the average hog was not on the kill floor at $8. It was probably hitting the kill floor at more like $25 a hundredweight for procurement. There was an extraordinary level of price spread in production that point in time. So certain producers got the worst witness on them and I think certain areas that have more of those smaller producers took a bigger hit.

I just wanted to mention support for packer ownership. I believe the Iowa Pork Producers Association just recently voted their support to ban packer ownership of livestock and Nebraska has continued their support for that. The Iowa Farm Bureau had a heated debate about it and I believe put some rather forceful language forward on it, as well. This is a debate that is really ongoing in a lot of farm organizations and commodity groups.

The last thing, just to mention rulemaking on discriminatory practices as it applies to contracting and captive supplies, once again those producers that were destroyed last year, or at least had their hog operations destroyed last year, one of the most significant things that they faced was not only an inability to get a fair price in the spot market but also an inability to get access to contracts. That is a discriminatory practice just as much as paying less for a hog, paying less just because you are small.

In the absence of the Packers and Stockyards Administration promulgating rules which define what these discriminatory practices are, including the extension of contracts, we are simply never going to have family farm producers, whether it be through contracting measures or through an open market, that will be able to survive.

And once again, to go back to USDA has simply been unwilling to do that rulemaking and needs to step up to the plate and do it.

The CHAIRMAN. Fine. Mr. Warfield, quickly, because I need to let Senator Roberts have a chance.

Mr. WARFIELD. The one comment on packer ownership of livestock, I should say that at the American Farm Bureau Federation (Farm Bureau) [AFBF] level, we do not oppose packer ownership of livestock but it does indicate a lot of differences among states and I have to say in Illinois, our delegates in December did pass a provision saying we would ban ownership of livestock by packers.

And I think this is indicative of the atmosphere we are in and I think it exhibits a frustration. And by states, we are doing what I think Senator Roberts said earlier. State by state, we are doing different things because of the concern that the action is not being taken at the national level.

The CHAIRMAN. I think your testimony helps us a lot. And just to complete the record, I am going to ask our staffs to first of all, try to give us an up-to-date census on who is still in the business, state by state and generally, so we agree on that and likewise, how many packers there are out there. There is pretty good information today about the percentage of capturing of these markets but we need to get up to date as to where the mergers are, who the people are and so forth.

Finally, we need a pretty good inventory of state action—legislative proposals, but also action by our major farm groups. As you say, a significant debate is going on in Iowa and Nebraska and elsewhere and as Senator Roberts commented earlier, this is important and some of our testimony is because if we have a checkerboard pattern ultimately, not just of opinions but actually of laws, sometimes that may opt against states that are passing these laws. We heard that a little bit with regard to price reporting in South Dakota, that the market dried up for a while, whatever may have been the merits of this in terms of a general policy.

Senator Roberts, will you please proceed?

Senator ROBERTS. Thank you, Mr. Chairman.

I want to thank all the witnesses for their excellent testimony. I think we are getting into this debate to the level that we should, as opposed to maybe the capsule comments that we see all the time in the press about this issue. I think all the witnesses have been very helpful.

I think the thing that is obvious to me is that as we go through this debate with our farm organizations and state by state, you have very strong opinions about this—it is the what-if—and I am really interested to see what could be done administratively, if it possibly can. You know, we are a very reactionary outfit back here and to propose legislation is certainly salutary but it takes a long time. You go through all the debates and then you have to dot all

the i's and cross the t's and hope that the administrative implementation works and it goes on and on and on.

I would really like to see what we could do from an administrative standpoint, so that is my two cents worth on that score.

John—pardon me—Mr. McNutt, you had indicated, I think on page 7 of your testimony, "Might there be a way of spelling out a few acts which constitute per se violations of the Act and thus save time and money and ensuring fair and competitive markets?" And you refer to a GAO study of the Secretary's authorities, duties and responsibilities which will address this topic.

I am aware of that study. I lost track of it. Where is that right now? What is the timing of it?

Mr. MCNUTT. September.

Senator ROBERTS. September. Is it going to be a one-armed GAO study so they cannot say, "On the other hand," like they normally do?

Mr. MCNUTT. Well, we will see, I guess.

Senator ROBERTS. That is a facetious question. I should not even have asked that. Thank you for your testimony.

Let me move on. Mrs. Sharma, I think your statement is very, very clear and it indicates the tremendous—what?—I guess the parameters of the debate. Do you think you and John Crabtree could sit down with a cup of coffee and figure this out? I think it does have some application here and I am not trying to perjure either one of you in terms of your statement. I think they are both very helpful.

But in Kansas we have the Kansas Livestock Association who has one position and the Farm Bureau is evolving. We have all sorts of other groups who recommend what John wants and then obviously you have some strong opinions, and that is why I think as we go through this debate if we could find out what we could do administratively, again, Mr. Chairman, from the standpoint of the administration, where they are and how we can help them, that would be better.

I do not have any specific questions, other than to thank you for your longstanding partnership in government.

Let me go to Mr. Roenigk and the chicken folks. You say on page 2, "With respect to one of the specific issues being addressed today, the National Chicken Council is opposed to the U.S. Department of Agriculture having expanded regulatory authority over poultry production because such additional power is unnecessary."

So red meat one way and leave our chickens alone? Is that about where you are on that?

Mr. ROENIGK. Thank you, Senator. As I noted in my testimony, there are a number of authorities that Packers and Stockyards has—the statutory trust, prompt payment provisions. Also, other government agencies such as the Federal Trade Commission and Justice Department have interest in our industry. And I also pointed out that our industry is somewhat different in structure with the contracts and there is contractual law that governs that.

So we believe we are somewhat different and we believe that our performance does not require additional regulatory authority.

Senator ROBERTS. Well, here we go again, Mr. Chairman. We have an all-encompassing problem and we have different segments

of agriculture saying, "Thanks but no thanks; we are getting along at least to the extent that we should." I think that is very noteworthy.

Let me go on to Ron, if I might, and I am going to try to hurry up because I know my time is fleeting.

You mention, Ron, in regard to page 2, "The Packers and Stockyards Act should be amended to" and you list five things that you think we should be doing. Oh, here is my answer. I was going to ask if that is the American Farm Bureau's position and you indicate that is the case.

Mr. WARFIELD. That is correct.

Senator ROBERTS. OK, thank you.

On page 4 you have indicated here that the "Farm Bureau would like to see an expanded role for the Department of Agriculture in evaluating agribusiness mergers and acquisitions currently required to be evaluated by the Justice Department. Broadened USDA responsibility and official consultation with the Department of Justice will ease much of the concern."

Mr. Stumo, on the other hand, has indicated in his testimony, if I can find it here real quick—I think it is on the last page of Mike's testimony, on page 9, I think; I numbered your pages for you, Mike—that you indicate we should transfer the anti-competitive—not should but could; I am misspeaking. What can Congress do? Congress could modify the Act to transfer the anti-competitive practices enforcement jurisdiction under the Act from the Department to the Department of Justice; consider the transfer of regulatory jurisdiction under the Act to another agency, such as the Federal Trade Commission.

Would both of you comment on that?

Mr. WARFIELD. I think I can comment. We had a meeting with the Department of Justice, Packers and Stockyards and USDA people back in September and what I saw reflected was when the specific concerns were presented by producers, we had a producer there who said, "I have a quality of hogs that meet the genetic requirement of a packer; the volume is not sufficient. I tried pooling with others, tried the pooling and networking concept and the packer would not accept it."

When we met with these groups, the Packers and Stockyards said, "That is Justice Department's problem." We went to the Justice Department and they said, "Well, that is over here." And we went on a ring-around all day, never knowing where we went for an answer.

So part of it comes back to a comfort zone of saying at least the USDA, we can go in and—and we want somebody we can point to and say, "OK, you are the ones responsible, you are the one that is accountable, we want an answer." And we feel like because of an understanding of the agricultural industry that the USDA having that involvement would be very, very helpful.

And I think that we are encouraged by the fact that the Justice Department now has put somebody that has dealing with agriculture, but on that day, as we went around, we could not find the person who we needed to talk to say, "Where do we get an answer?" And all they did was point to another agency, and the Federal Trade Commission was one of them that we got to. And we,

today, do not know—when we tried to evaluate what a live hog is worth and the retail pork prices and trying to say what is going on here, we cannot find out information to get the answers; we cannot find the Agency that is supposed to be responsible to get it done.

So if I had to come back and answer most simply, let's very clearly identify authority and responsibility, where we go to, and say we have to have the answer, and quit the finger-pointing between the different agencies.

Senator ROBERTS. Michael?

Mr. STUMO. Senator Roberts, Mr. Warfield and I start in the same place and the reason I think we go in different places is my view of the issue is that who does what best. USDA has, as a cultural matter, they have a conflict of interest in that they promote agriculture and they regulate it.

Now, let's look at the specific task at hand, which is anti-competitive practices, which is not necessarily antitrust. It is rules of competition. And we have, as we saw today and as Mr. Warfield said, we have Justice and USDA pointing their fingers at each other. So what do we do?

Justice works with anti-competitive practices cases or antitrust cases all the time. They have a methodology. They have developed internal guidelines to determine when they collect information. They know what a dog is when they see it. They have the guidelines to do that. P&S does not. OGC does not.

This Committee has been frustrated by inaction. The producers in the field have been frustrated by inaction. Mr. Dunn has mentioned the rapid reaction team that runs around in pursuit of rapid responses to problems identified. I have talked to the producers who talk to these rapid reaction folks. The message they get is we cannot do anything. We do not know whether this is a violation. It is too big. Just do something else. It will take years to do something about.

They are met with obstruction at every step of the way and the fact is that GIPSA cannot handle it. The people in government who are good at this sort of thing do not go to GIPSA. They go to FTC or they go to Justice. And the legal counsel that are good at this sort of thing do not go to USDA OGC. Other people go to USDA OGC. But for competition policy, the good people go to Justice, and that is why I would consolidate this type of authority in Justice. Thank you.

Senator ROBERTS. Mr. Chairman, I am going to ask John my last question here and then we can—I know we are running out of time.

Mr. Crabtree has indicated a vision of the future of rural America dotted only with packer-owned industrial hog operations is untenable and I certainly agree with that. He cites the work of the Center for Rural Affairs in the past, being a catalyst for legislation in states, and this gets back to the original statement that I made when the hearing started that if the Federal Government does not respond, states do. Then you get into a situation, as described by the previous witness, I think from Indiana, that if you get an isolated situation, you do not know what is going to happen in regard to the next state over and it gets to be a real hodgepodge.

John also pointed out, and I am not trying to give your testimony again here, John, but he cites the letter from Professor Neil Harl of Iowa State, who is a renowned authority on agriculture policy, that "The USDA has not fully exercised the authority granted under the Packers and Stockyards Act to promulgate rules, especially in the area of discrimination in livestock pricing. Professor Harl has also pointed out in the past that courts will give an administrative agency leeway in enforcing market regulations if they promulgate the rules."

And I think Mr. Crabtree is pointing out once again that if we can get some action here, I know the GAO report is due in September and I know that the gentleman who came down from the department will respond back to the Chairman but in the meantime, if we can get some kind of a policy here where we can take action from an administrative standpoint, that might relieve the pressure just a bit.

I have made a speech, John. I do not know if you want to respond to that or not but I will certainly give you the opportunity.

Mr. CRABTREE. I think that is absolutely right. Two years ago Secretary Glickman's own Commission on Small Farms asked him to take action on price discrimination. We put the same issue before him last year, in August. We talked about this time and again and I think you are absolutely right. This is something the administration can do now, the Secretary should do now. They can issue these rules and move, move forward to making this market more competitive.

I want to say one thing about the unintended consequences of states versus states. Nebraska has had probably the toughest prohibition on packer ownership of livestock in corporate form for 17-years. We are also still the number one producer and processor of red meat in this country.

So I think the connection of losing packing or losing production does not always have to follow on with where vertical integration goes. I think you can prohibit packer ownership and still have a healthy livestock industry, as we do in Nebraska.

Senator ROBERTS. I would like to compliment Mr. Stumo. This is his first opportunity to testify, as he has indicated. He was very specific, Mr. Chairman. He lists probably 10 or fifteen things that we could do. Most witnesses will testify and offer some very important information but he actually gets very specific. I am not saying I am for each and everything that he is recommending but I want to thank him for that.

And the only thing that I would warn is that I have a bias, Mr. Chairman. Obviously, I think I am biased, since I am a piece of old furniture around here, but I would like for the Department of Agriculture, once you give up jurisdiction in behalf of agriculture and farmers and ranchers to other agencies, I think you leave the dock and you are into uncharted water.

And whether it is global warming and EPA and the USDA, where we are trying to get the USDA to step up to the issue or whether it is trade that the distinguished Chairman is such an eloquent spokesman of and a leader for in regard to the National Security Council and the State Department making decisions on so-called sanctions reform that are not sanction reforms because we

cannot use the export programs that we need to use, or whether it is this issue, it seems to me that the department should take a much more aggressive role and get that jurisdiction within the Department of Agriculture so it would not be necessary to follow the advice that Mr. Stumo feels is necessary.

I thank you for your leadership again, Mr. Chairman. It has been an excellent hearing.

The CHAIRMAN. Well, I second the motion, Senator Roberts. I just seems to me clear that so much could be done through administrative action and we know whatever our role as legislators may be, it is a two-house procedure, signature by the president, endless amendment.

To the extent that we really are able to do some rule-making to move ahead, I voiced at least some of my frustration over that we have been commended for our Price Reporting Act last year but we find that all sorts of pieces are not happening because an appropriation did not occur here, $500,000 missing here.

In essence, this is a frustrating business. You can pass an act. You can get bipartisan support. You can work it all out and it does not necessarily happen.

So it has to happen. I feel very strongly about that. I want USDA to find out why it is not happening and where the money can come from. We may have to mandate a transfer within USDA to get it done but we really are determined finally, that the people's will be heard.

Now, you have been most constructive and helpful and I commend you for your patience; likewise the audience, who has stayed with you and are deeply interested. But at this point I will ask you to retire and we will have the fourth panel, who are Mr. Bert Farrish representing the North American Export Grain Association from Portland, Oregon; Mr. Robert Smigelski representing the National Grain and Feed Association from Maumee, Ohio; Mr. Mike Clark, National Corn Growers Association; and Mr. Dennis Wiese, National Farmers Union.

May we have order in the Committee room so that we can proceed with these witnesses?

I will ask that each of you limit your testimony, if possible, to 5 minutes so that we can proceed with a colloquy with the Committee and everyone can be heard. I will ask you to testify in the order that I introduced you; first of all, Mr. Farrish.

STATEMENT OF HUBERT FARRISH, PRESIDENT, COLUMBIA GRAIN, PORTLAND, OREGON, REPRESENTING THE NORTH AMERICAN EXPORT GRAIN ASSOCIATION

Mr. FARRISH. Thank you, Mr. Chairman and members of the Committee.

The export grain industry appreciates the opportunity to present its views on the role, function and performance of the Federal Grain Inspection Service. This hearing is timely, since five sections of the Act that authorize FGIS expire September 30 of this year.

I am Bert Farrish. I am president of Columbia Grain, Inc. headquartered in Portland, Oregon. Columbia is an exporter of grain primarily to Asia and the Middle East and we are one of the largest users of the services provided by Federal Grain Inspection

Service in the United States. Today I am testifying on behalf of the North American Export Grain Association, an industry group that represents U.S. grain exporters and associate members.

In my testimony today I will discuss what I think this agency is doing well, how the Agency could improve, and the challenges for the future. I will present an abbreviated version of the written testimony and would ask that the written testimony be entered into the record.

A little background. The Federal Grain Inspection Service was created in 1976 to administer a uniform national grain inspection and weighing program, as required by the U.S. Grain Standards Act. The Act provides that official inspections of grain are mandatory at export and voluntary for domestic shipments.

I would like to make a few remarks regarding FGIS operations. In the view of exporters, the Federal Grain Inspection Service has two broad missions. The first is to directly provide the service of inspecting and weighing grain for export or to supervise delegated state agencies that provide this service; and second, to provide the structure and administration of the Grain Standards Act, which benefits all producers, processors and consumers. So my remarks will be made in the context of those two broad missions.

First, what are some of the successes of the Federal Grain Inspection Service? The FGIS weight and grade certificate has great credibility and integrity with importers worldwide. U.S. exporters want to protect this integrity. The Federal Grain Inspection Service has responded to industry cost concerns by reducing total staff and lowering the cost per ton for providing service. Number three, FGIS is working with industry on a broad range of important issues. And fourth, FGIS has communicated well with the grain trade through its advisory committee and various industry committees.

Second, what are some of the areas of concern or need for improvement with the Agency? First, the struggle for cost control and improvement will never end. As long as the industry perceives itself paying excessive fees for export service, there will be pressure to reduce costs. We need cost control, but not at a loss of certificate integrity. And I would commend the Agency for absorbing part of a recently proposed fee increase through improved efficiencies, but we look for more improvement.

As a government agency, FGIS operates by a different set of rules than the private sector does. Operating costs for this agency are far higher than would be the case for a similar private sector provider.

Also, FGIS needs more freedom to develop operating flexibility. The grain trade, particularly at export, is ever-changing and needs flexibility to adapt and compete.

Third, we can improve communication through existing formats, particularly concerning research that the Agency is contemplating conducting.

And fourth, we need to better address the funding that supports what we see as FGIS's dual functions. Those functions are to, first, act as a direct service provider at export, and second, to provide broad regulatory oversight of the grain industry.

The agency is funded by two methods. The first is user fees; the second, appropriated funds. In our view, it is critical that appro-

priated funds are readily available for the support of standardization and methods development activities. The U.S. exporter, who is a mandated user, cannot continue to shoulder more in user fees than its fair share.

And lastly, the time required for changing procedures and regulations needs to shrink to accommodate the faster pace of change in business.

And lastly, I would like to talk about the future a little bit. This is an exciting and challenging time for both U.S. producers and exporters. In the future, GIPSA should work closely with all segments of the grain industry to, first, be prepared to provide GMO trait testing as the market may require; second, to identify and provide the testing of end use value characteristics of U.S. grains; third, to continue developing technology that lowers costs and improves delivery of services and data; fourth, to identify e-commerce opportunities; continue to identify and conduct research that benefits the grain industry; and last, to continue to improve contacts with grain importers worldwide.

I would conclude by saying that the export industry needs GIPSA-FGIS to be a cost-effective, forward-looking business partner that assists U.S. producers and exporters in expanding our world market share. We think that FGIS is a critical link in the success of the U.S. export grain trade. That concludes my testimony, Mr. Chairman.

[The prepared statement of Mr. Farrish can be found in the appendix on page 141.]

The CHAIRMAN. Thank you very much, Mr. Farrish.

Mr. Smigelski?

STATEMENT OF ROBERT SMIGELSKI, THE ANDERSON, INCORPORATED, REPRESENTING THE NATIONAL GRAIN AND FEED ASSOCIATION, MAUMEE, OHIO

Mr. SMIGELSKI. Mr. Chairman, my name is Robert Smigelski. I am Agriculture Group Operations Manager for the Andersons in Maumee, Ohio. I am representing the National Grain and Feed Association and serve as that organization's chairman of the Grades and Weights Committee. We appreciate the opportunity to provide input on the Grain Inspection, Packers and Stockyards Administration and will focus our comments on the Federal Grain Inspection Service, a program within GIPSA that administers the U.S. Grain Standards Act.

The NGFA has a strong and long experience with FGIS operations, including its official standards and grades. Furthermore, NGFA members operate both interior and export facilities. These factors provide us with a broad and deep perspective on FGIS services in both the domestic and the export markets.

We support the Agency's efforts to maintain accuracy and consistency in the official inspection and weighing system. The credibility and integrity that FGIS strives to maintain in the official system is very important to grain handlers and very beneficial to the exporters in the United States.

FGIS and industry maintain a positive working relationship. Agency management routinely meets with us to discuss issues affecting the official system.

We appreciate agency efforts to increase the efficiency of U.S. grain marketing, streamline grain inspection and weighing, and provide cost-effective grain inspection and weighing services. In this regard, the Agency has been working with industry to improve automation at export facilities, an effort we applaud.

Recently FGIS announced plans to establish a reference laboratory in its Technical Service Center in Kansas City, Missouri to verify the accuracy and repeatability of test kits used to detect biotechnology-enhanced crops. We believe this service will be beneficial to industry and we support this effort to increase the kind and the amount of service the Agency provides.

While the Agency is working in a positive way to meet its mandate under the U.S. Grain Standards Act, we think that the 2000 agency reauthorization provides an opportunity for industry and Congress to consider some potential changes in the official inspection system that could be beneficial. Let me share with the Committee our thoughts on several of these issues.

The cost and efficiency of official service in domestic markets has been a concern to NGFA members. To determine if market forces could be successfully used to address this issue, the Agency began a serious series of pilot programs in 1995 to open selected interior official territories to competitive bidding for service. We support these pilot programs and believe the results justify granting FGIS permanent authority to allow increased competition within the domestic official system.

The cost of official services is also a concern at export elevators. Since FGIS must provide personnel for the bulk of official services at export facilities, a series of fee increases instituted by FGIS over the last several years has impacted more directly on the exporters. In fact, one of the top expense items of the export elevators is the cost of inspections. While the Agency reported improved financial performance in the fiscal year 1999, the cost of official inspections at export locations and future management of those costs remain a concern.

To address this situation, one option under serious consideration by the National Grain and Feed Association would be to shift FGIS from a more traditional government agency model to a performance-based organization, PBO, within the Government. The PBO concept was designed as a business model for government agencies heavily focussed on service to the private sector, a description that fits much of FGIS operations, as well.

While several questions remain, we believe the PBO concept could offer FGIS greater flexibility in the way it manages its operation while retaining strong Federal Government oversight on the inspection functions.

Another policy option to consider is reducing the 40-percent cap on administrative and supervisory fees to a 20-percent cap. Reducing the mandated cap on overhead costs would be consistent with trends within private industry and may also be consistent with trends within the Agency itself.

Lastly, given today's rapidly changing global business environment, we think that the seven-year period incorporated in the 1993 reauthorization was simply too long. Rather, we recommend that

Congress consider reauthorizing the Agency for no more than 5-years.

Thank you, Mr. Chairman, for the opportunity to testify. I will be available to answer questions.

[The prepared statement of Mr. Smigelski can be found in the appendix on page 151.]

The CHAIRMAN. Thank you, Sir.

Mr. Clark?

STATEMENT OF MIKE CLARK, VICE PRESIDENT, ILLINOIS CORN GROWERS ASSOCIATION, REPRESENTING AMERICAN SOYBEAN ASSOCIATION NATIONAL ASSOCIATION OF WHEAT GROWERS NATIONAL CORN GROWERS ASSOCIATION, HOMER ILLINOIS

Mr. CLARK. Thank you, Mr. Chairman. I am Mike Clark and I currently serve as vice president of the Illinois Corn Growers Association. I raise corn, soybeans and wheat near Homer, Illinois and Vedersburg, Indiana.

It is my honor today to appear before you on behalf of the American Soybean Association, the National Association of Wheat Growers and the National Corn Growers Association.

As a farmer, my operation is directly impacted by the work of GIPSA and the grain standards it enforces. As we enter the new century, we should take the time to review how our government operates and ask ourselves: is there a better way? This certainly applies to GIPSA and the standards it enforces. Indeed, many of the grain standards are nearly a century old themselves, having been created by the Grain Standards Act of 1916.

While GIPSA is to be commended for its efforts in modernizing its operation, little has been done to bring grain standards into the 21st century. As you well know, U.S. producers must export a significant portion of their crop each year to remain solvent. This requires us to compete in a world market against well-positioned competitors. Across the globe, world grain buyers have grown more sophisticated in their buying requirements, yet we continue to rely on standards that largely only describe external characteristics.

Current U.S. grain standards measure only volume and outward appearance. Very few inspection standards exist to give grain buyers the information they really want: the end-use characteristics of the crop. Farm groups, this Committee and the Agency need to engage in open dialogue to determine if these needs are to be met by the public or private sector.

Take, for example, how we measure protein in wheat. While wheat is graded by the amount of protein it contains, no standards are available to measure the quality of the protein or the gluten content. Tests and standards need to be developed to identify the inherent traits that bring about the highest end-use value and help identify and preserves true wheat quality.

Millers and bakers want to know how the wheat they purchase will grind into flour, how it will bake into bread, and how it will affect the quality of their product. Without making changes which reflect end-use quality, U.S. grain producers will be left flat-footed on the world market, unable to capture the true value of their product.

To its credit, GIPSA has made some advances in this area. However, much remains to be done. We need to harness the continued advances being made in technology to bring about a reliable and quick test that will predict the intrinsic qualities desired by the end user. In addition, we must retain the flexibility to adapt such standards as new technologies are developed.

These issues are made even more complex when we consider the growth of biotechnology. For example, consider for a moment how biotechnology is currently affecting the corn industry.

Biotechnology is clearly the single largest driver of change for the corn industry. As such, it will be important for all segments of the industry—producer, processor and regulator—to define their new and different role in this era. The rate of change spurred by biotechnology is so rapid that we cannot rely upon the time-tested practice of defining policies based on the experience of the past but rather, by anticipating the needs of the future.

We are still defining the regulatory expectations of GIPSA and other government agencies in that future. We do anticipate that in the future the opportunities for corn farmers to extract additional value from the drop will arise from being able to move up and down the value chain. This means we will need to better know and identify the intrinsic qualities of an increasingly segmented corn market—a marketplace where farmers, handlers, processors and customers will be tracking, testing and identity-preserving individual loads of grain.

In this new arena, standardization of tests and testing equipment will be vital. GIPSA can play an important role in making sure that tests for intrinsic qualities are timely, repeatable, verifiable and of a nature that can be used by commerce in our country elevator system.

Likewise, the soybean industry is actively considering the development of testing and analytical procedures for a variety of traits derived through both commercial breeding and biotechnology. These traits include high content levels of oleic and stearate fatty acids, low linolenic acid content, low phytate content, and high sucrose content. Soybean growers are working with other industry partners to develop standards for these characteristics for recommendation to GIPSA.

The impact of biotechnology on the grain trade and, in turn, our expectations of GIPSA is currently evolving. We are still exploring our expectations of contracts, grades and standards in the future. While we cannot say today with certainty our expectations for GIPSA in the future, we look forward to dialogue with the Agency and this Committee to clarify that role.

Meanwhile, we must continue to monitor and improve GIPSA's everyday operations and the grain standards we currently have. It is vitally important that, in addition to the current user fee system, GIPSA continue to also be funded by appropriated Federal funds. The standardization and development of tests, as well as other related GIPSA activities, benefit society at large and should be funded by society rather than through user fees.

Just this year, GIPSA developed standards for a new class of wheat—hard white. It is to be commended for working with wheat producers and commissions from across the country to develop reli-

able, workable standards that will help guide the development of this class of wheat across the Midwest.

While not all producer groups are in agreement, the National Association of Wheat Growers commends GIPSA and its partners at the Foreign Agricultural Service for their efforts in advancing USDA's grain cleaning initiative.

Again, Mr. Chairman, let me thank you and the Committee for the opportunity to appear before you today. I appreciate your timely evaluation of these concerns.

[The prepared statement of Mr. Clark can be found in the appendix on page 154.]

The CHAIRMAN. Well, thank you, Mr. Clark.

STATEMENT OF DENNIS WIESE, NATIONAL FARMERS UNION, FLANDREAU, SOUTH DAKOTA

Mr. WIESE. Thank you, Mr. Chairman. My name is Dennis Wiese and I am president of the South Dakota Farmers Union and I also represent the National Farmers Union today.

First, let me say thank you for last year's price reporting initiatives. While I want to confine my comments to the FGIS issues, I think it is worth noting that your efforts here have made a big difference as to the plight of the farmers in the countryside.

I testified in South Dakota in Federal court and had to go through the issues of whether price reporting was important to producers, and they find it very important. It is only one piece but it was certainly a huge step, one that yes, the states had to take initiative. The Federal Government, through congressional action, did not happen, even though it was in the body back in 1995 by Senator Daschle, but I do commend you and this Committee for helping move that forward.

Also, I would like to also refer a little bit to what could be enhanced on that before I go on. That is that inside of the price reporting there needs to be an identification of the differential pricing. Differential pricing is not prohibitive or wrong necessarily but if it becomes discriminatory in that process—and that is where I think both USDA and our own attorney general in South Dakota have identified some needs to determine whether or not there is actual inappropriate practices being applied there.

Now to the Federal Grain Inspection Service, which grades—they become the basis for determining our adjustments to the final settlement of sales agreements between the farmers and the merchandisers and in transaction between the merchandising sector and domestic processors and our overseas customers.

In order to ensure objectivity and accuracy in fulfilling this mission, FGIS engages in research and development activities to review and test new procedures, standards and technology, provides ongoing education for inspectors, and engages in monitoring its performance and output against other grain inspection systems.

A user fee system that is periodically modified has been established to recover a significant portion of the cost of the services provided by FGIS. However, as with the majority of the marketing expenses associated with the grain sector, the producer, directly or indirectly, pays the cost of those inspection services through adjustments to the price received at the farm-gate. The farmer thus has

a strong vested interest in the efficiently run agency that adopts, consistently applies and enforces standards that enhance the marketability and the competitiveness of U.S. grains to achieve the highest level of consumer satisfaction.

In the new decade, significant economic challenges confront grain producers that are related to the mission of FGIS. These challenges include the traditional issues of agency service levels, modifications to standards, dispute settlement and user fees. In addition, FGIS must adapt to emerging considerations that are the result of increased competition for markets and market share. These issues include grain cleaning and new production and product technologies.

The issue of grain cleaning takes on new significance in a global market where many forms of intervention have been reduced that, in the past, have been used to offset market advantages associated with large-scale commodity cleaning requirements and operations. In addition, the increased market power associated with highly concentrated and integrated multinational merchandising and processing sectors allows these companies to play differing national marketing systems—*i.e.*, those that require grain to be cleaned versus those that do not—against one another to the disadvantage of grain producers globally.

We believe the U.S. should utilize a portion of the budget savings associated with those reductions to implement a grain cleaning pilot program to test the effectiveness of such a system, including its customer relations impact.

Some may view this approach as unnecessary and undesirable intervention on the part of government that is not supported by the marketplace. However, many of those same opponents directly benefit from the business generated by systems engaged in grain cleaning and/or creates additional company profits by blending various grades of U.S. grains that have been purchased from the producer at a discount already.

New technologies, such as genetic manipulation of grain crops to achieve specific production or physical attributes, raise serious grain inspection issues. These include certification as to the presence or absence of GMOs, product segregation, and the potential for and vesting of liability in the event of misidentification of bioengineered crops.

Unless and until all nations reach agreement on the conditions of acceptance of these crops, and cost-effective, efficient testing procedures are developed consistent with such an agreement, regulatory agencies and producers will remain at risk. The FGIS in its certification role will be challenged in terms of its credibility. U.S. crop producers will ultimately bear the market risk of the technology through the imposition of domestic and international market barriers, price discounts, and potentially legal liability. The majority of economic benefits associated with biotech will flow to those with the greatest level of multinational integration.

We support congressional action to ensure that producers of genetically enhanced agricultural products are held harmless from any legal liability that may result from the production or marketing of these products and that producers should not be responsible for the cost of any testing requirements that may be imposed.

In addition, we support cooperative international efforts to ensure consumer confidence in the ag products they purchase, including the establishment of a labeling requirement to allow consumers the ability to make informed purchasing decisions.

Finally, the market for GMO products is likely to require a much better system product segregation than currently exists in the U.S. We would encourage on-farm grain storage facility loan programs to be utilized, as well as a limited farmer-owned reserve program.

Thank you for your time and I would be happy to answer any questions.

[The prepared statement of Mr. Wiese can be found in the appendix on page 159.]

The CHAIRMAN. Thank you very much, Mr. Wiese.

I want to take advantage of the expertise of this panel and the organizations you represent. First of all, clearly you have all talked about the need for standards that recognize something beyond external appearance. I suspect that probably that is understood by FGIS, by USDA, but the usefulness of this hearing is once again, in a more high-profile way, to indicate the changing needs of marketing in our country, given the opposition that we have elsewhere.

Likewise, the grain cleaning situation we heard talked about a little earlier in the testimony this morning with a lot of conflicting testimony, as the gentleman said, but that does not mean it is put to rest. The USDA at least is engaged in those hearings and coming to some decisions. And, as Senator Roberts stressed a number of times, some administrative policies could be adopted here that would be very helpful. Our Committee is very interested in that, as you are, and I simply want to acknowledge that interest and follow-through that we shall try to bring to bear.

I want to ask, however, as a topical situation, yesterday I had a long press conference and gave a first impression of this Biosafety Protocol that the United States acceded to the day before and my feeling about that was very adverse. As I note in the press today, some of my comments seem to run counter to others from grain organizations, some of which are quoted as saying it is really not so bad or it will not have that much effect.

But I found in the World Perspectives, Incorporated Ag Report today, in a piece written by Gary Blumenthal, and I give credit to him; he points out that the United States agreed to sweeping controls over the movement of these grains. He said, "Advanced, informed consent will be required before shipping genetically modified seed and before shipping grains for consumption in instances where a country lacks its own regulatory controls. Grains that contain genetically modified content must be labeled 'May contain' until more detailed labeling requirements are negotiated within 2-years and the precautionary principle applies even to countries that do not have to show scientific certainty before blocking imports of food they believe could be harmful."

Specifically, he says, "Countries may consider adverse socioeconomic impact in considering whether to block imports of genetically modified food. The Biosafety Protocol is not subordinate to any other agreement, since it occurred later in time than the Uruguay Round and therefore could be considered superior in international law."

Now this newsletter says "The breadth and depth of capitulation by the United States is shocking. There is even an exemption for pharmaceuticals for humans, as though the biotech process is only dangerous in food, as opposed to drugs." This appears to me, as people begin to allow these to seep in, pretty serious business.

We have talked today prospectively about the need for standards, the need for the marketability of what we are doing. We have this pilot project or the beginning of this laboratory that may give us some idea of to what extent a shipment of grain has biotechnology or it does not. We have heard testimony before this Committee that this is difficult to detect with the precision that some are requiring; namely, 99-percent pure, less than 1-percent biotech. And, as a matter of fact, that much grain—some have even said most grain in the United States—may have a touch of biotech after three or four or 5-years the fields and pollination and so forth. It raises very real questions for USDA if there are premiums for the nonbiotech suddenly and quite a distortion in price.

For example, we still have LDPs, we still have loans. USDA, the Government could just stuck with a lot of grain sitting around that suddenly does not have the markets that we anticipated because countries are saying we have a socioeconomic bias and we are busy and eager to take any pharmaceuticals you have because they are life-saving but we have a protectionist policy with regard to grain. And you have acceded to this protocol, so you are stuck with it.

Now, this would appear to me to be something that needs boards of directors meetings pretty generally with people who are representing grain farmers in the country, to see what is going on here and what is to be done. Clearly, the obligation by FGIS is enormous.

If there has to be proof before a country will accept a grain shipment, who says this is perfectly fine? The country may not have any grain inspection of its own, so it says to the United States, "Prove it." Well, somebody has to do the proving, presumably FGIS or somebody's laboratory back here that can certify this before the shipment is made. Or at least it could be challenged if such a shipment is made without that certification.

So I ask any of you for some general impressions as to where we are and what additional things we ought to be visiting with FGIS about, given this enormous change, I think, in the lay of the land with regard to exports of bulk grain from this country that are implied by this protocol. Does anyone have a first impression? Yes, Mr. Wiese?

Mr. WIESE. I have never been short for words, Mr. Chairman. I guess what we have is massive confusion amongst the farmers.

First of all, their concern is who are the consumers that they are supposed to be supposedly producing for? They were told to supply the genetically modified stuff and lo and behold, we really do not have a market for that. So I think that is their first concern. There are no premiums paid to any farmer for any of that stuff; never was. So that never existed.

And I think lastly and probably most importantly is if there is an identification of that type of commodity commingled, who is going to be held liable in the cases of the repercussions, whether they come from domestic or international partners?

I think those are all very pertinent issues and things that we believe should be addressed through FGIS so that we have some standard. Ultimately I assume they will respond with some state agency being a partner on that, as well.

The CHAIRMAN. I think those are very relevant questions, I suppose some that might have been asked before we acceded to the protocol, but nevertheless still very relevant now that we are in this fix.

Yes, Sir?

Mr. SMIGELSKI. We are still struggling with what the market is. Is it biotech or is it nonbiotech? And very bluntly, in order to do a good job of testing the grain at the elevator level and at the export level, we do need an agency such as Federal Grain Inspection to do that, but they are simply testing the test. They are making sure that they do measure what they are measuring.

The industry is providing this from the various sectors, but what we need is we need a very quick, very reliable means of testing that will consistently, over a consistent period of time, measure exactly whether it is biotech or not. The challenge is to get one that we can depend on and one that will do it quickly.

The CHAIRMAN. Now, we do not have one now?

Mr. SMIGELSKI. Well, we have one—we have several, but they can be questioned. There are questions. You take a one-minute or two-minute test and then you take a three-day laboratory test that is more scientific and has a longer period of time to come up with the conclusions and it may prove a positive reading to be negative or vice versa.

The CHAIRMAN. Well, as a practical matter, what happens then if country X says, "I do not think your test is very reliable"? In other words, you are asserting that this is pure of any biotechnology but how do we know?

Mr. SMIGELSKI. Well, we are doing very much the same thing that we are telling the farmer. We are telling the producer that before you plant, make sure that you have a market. And before I contract with a foreign country about whether it is biotech or not biotech, I want to know what the parameters are and which test will serve as, let's say, the ruling test. So we try to do that in a contract.

The CHAIRMAN. Now, getting back to Mr. Wiese's question, if I am a corn farmer in Indiana or he is a corn farmer in South Dakota or what have you, do we then try to find out the destination of the corn from our farms? In other words, there is no way we can do that.

Mr. SMIGELSKI. Right.

The CHAIRMAN. So where do we get the signal, then, as to where there is a market for all this?

Mr. SMIGELSKI. What we are doing is we are advising the producer to check with his market. He has to check with the elevators that he plans on delivering the grain and say, "Are you taking this commodity and are you paying a premium for it or aren't you?" The biggest concern they have today is whether they will take it.

The CHAIRMAN. Yes. But it at the elevator level, then. So if you are able to make the sale to the elevator, you are home free as a producer. Then it is his problem.

Mr. SMIGELSKI. Right, but that is the problem. We are struggling, my company itself, we are struggling with what we are going to do with all the biotech grain.

The CHAIRMAN. Sure. I am worried about my elevator at Beech Grove as to what sort of a struggle they are going to have.

Mr. SMIGELSKI. I agree. You should worry.

The CHAIRMAN. Yes, Sir?

Mr. FARRISH. Mr. Chairman, just to speak briefly on the Biosafety Protocol, initially when I read the article in the newspaper concerning it, I thought well, this does not look too bad if all we have is some "may concern" language. But I think the further we get into the agreement and as North American Export Grain Association [NAEGA], looked at the agreement, we are not comfortable with this agreement.

The CHAIRMAN. No.

Mr. FARRISH. We think it presents us some real problems with exporting grain. Like the others, I would describe the industry as basically feeling its way through a dark cage on this and really not knowing where we are headed. My firm is not engaged currently in the corn and soybean business but trust me—in the wheat business, we are standing back and watching what happens here very carefully because we know we are probably best for the biotech arena.

With regard to FGIS, while they do not do the tests directly, they are in Kansas City, in the Technical Center there, developing testing procedures to test the validity, if you will, of the testing kits that private companies are providing the industry, but testing at the tailgate, at the country elevator, will never be the solution to this problem, not in the near future, because the tests take too long to run and no farmer or country elevator wants to be subjected to that type of time.

I would suggest that our organization believes that the answer to the problem lies in harmonization of the standards, acceptability standards or standards for accepting these products worldwide. We need somehow, through our trade negotiations, to get to some harmonization of the procedures and the regulations for these crops. Then we think we will have the problem behind us.

And there are still many who believe that this industry can successfully segregate Genetically modified organism [GMO] and non-GMO prompts, and we do not believe that, that is really feasible. There is too much risk in the transportation and handling system for contamination back and forth between the two to really make this possible.

If we did try to make that possible, the expense would be enormous. It would require building two separate handling systems and transportation systems for grain products.

The CHAIRMAN. Well, that is the testimony we have heard before here, that ultimately this is a gesture in futility while we are all busy trying to parcel all this out, and your point, I think, is the right one. Our trade negotiators have got to do a better job. You know, we cannot accept one disaster after another in this area, but that is for another hearing at another time.

Mr. Wiese, you were trying to——

Mr. WIESE. Well, from the standard for the farmer who delivers to that small town, who then has that product delivered to another facility, he may deliver to a coop who has an alliance with a private institution that then takes it to a port that neither of them control through a transportation system that may have different commodities handled in it previously. I think at some point you have to determine what is an acceptable level, if any at all, much as we do on other grain standard issues.

Then I think the other thing is you could do it at the local level, much as we do protein levels. You could do it also much like we do in a livestock setting with a grade and yield. We will pay a certain portion for every bushel out until the test returns.

The CHAIRMAN. Mr. Clark, do you have any comment on all this?

Mr. CLARK. Yes. As a producer, obviously we are in a state of transition but on the Biosafety Protocol, that will not deter us from our overall support of biotech. Planning decisions are unique individual risk management decisions for the individual producer and the first job should be to get—a good step would be to get the standardization of tests so that the results could be acceptable for everyone.

In Illinois, in our corn growers organization, we have put out booklets to our members that basically say, "Know before you grow. Know what your customer wants. Know who your customer is." We have a map of the state and have circles on the different buyers and users in the state and what they are wanting to have.

We have Staley's in Decatur and Lafayette, Indiana coming out and saying they do not want GMOs for fall delivery. ADM, the question is still out on them on whether they will use those in their processing plants, whether they will accept them at the river terminals. Frito-Lay elevator near my home in Homer came out last week saying they wanted to go non-GMO. Lalhop in Danville is still on the fence and that is one of my biggest customers. Then my local elevator in Homer is owned by them. They do not foresee a problem right now with GMO crops because their biggest customers are in the Southeast, the poultry and pork industry.

But the biggest thing for producers is to know who your customer is; that is who you are producing the product for; that is who is paying your bills ultimately for you, and to grow what your customer wants. That decision should be left up to an individual farmer as far as his risk management program.

The CHAIRMAN. Well, I thank each one of you. Let the record show that you all lasted for 4-hours and were still cogent and wise even after that period. We look forward to staying in touch with each of you.

These subjects, we will revisit and I appreciate all witnesses who have come today.

The hearing is adjourned.

[Whereupon, at 1:03 p.m., the Committee was adjourned.]

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APPENDIX

FEBRUARY 1, 2000

WAYNE T. GILCHREST
1st District, Maryland

COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE
CHAIRMAN, COAST GUARD AND MARITIME TRANSPORTATION
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Statement of the Honorable Wayne T. Gilchrest
Before the Senate Agriculture Committee

February 1, 2000

Mr. Chairman, I am pleased to be here today to talk about an issue that is very important to the 30,000 poultry growers around the country and the nearly 3,000 growers on the Delmarva Peninsula.

While concentration of the livestock industry has brought some positive developments, such as larger economies of scale, we must also be consider of the effects on individual producers. Presently, there is an inequity within the U.S. Department of Agriculture's oversight and enforcement of violations by poultry companies. I am here to seek your support and assistance in addressing inequity.

In 1921, Congress passed historic legislation known as the Packers and Stockyard Act, to protect livestock producers from unfair, unjustly discriminatory, or deceptive trade practices. In 1935, Congress amended section 202 of the Act and made it unlawful for "any live poultry dealer" or company to engage in these same practices, placing them under the same regulations as meat packers. However, the amendment failed to include the term "live poultry dealer" in the next three sections which permit administrative enforcement authority for violations of section 202.

What this basically means is that Packers and Stockyard can investigate violations by poultry companies but cannot bring administrative action against alleged violations, which they are able to do for cases involving the beef, hog and sheep industries. The Department must refer poultry cases to the Attorney General for prosecution. As we all know, the dockets of districts courts are overloaded, leading to delays in prosecution of violations of the Act and significantly increasing the cost of litigation for both the Department and the poultry company. USDA officials have also explained to me that because the federal courts lack expertise in these areas it is often much more difficult to prove these cases. The current law has discouraged USDA from following through on many cases of violations because of these extra hurdles, and that is not right.

I, along with the support of some of my colleagues, have introduced legislation to give USDA administrative authority to address unfair practices against producers. This would enable us to pursue violators quicker and cheaper, providing all producers the full protection of the Act as well as swifter resolution of cases for alleged violators.

This legislation would ensure that all livestock producers are afford the same protections under the Act and ensure that meat packers and poultry companies be subject to the same administrative enforcement. I believe this was just an oversight, and we need to act quickly to end the inequity and ensure fairness; my constituents deserve no less.

I know that Secretary Glickman strongly supports this effort, and I am sure that his representatives here today, can give you more specific reasons of why this legislation is so important.

I appreciate the opportunity to share with your my thoughts and efforts. I would be happy to answer any questions.

Opening Statement of Chairman Richard G. Lugar, a U.S. Senator from Indiana, Chairman, Committee on Agriculture, Nutrition, and Forestry

Agriculture in the United States is experiencing a significant transformation. This evolution can be attributed to rapidly improving technologies, developments in biotechnology, changes in worldwide consumption, and concentration in production agriculture and agribusiness. These developments create opportunities, but raise questions about concentration and antitrust. The developments also raise new challenges in the regulation of unfair and deceptive business practices, and identifying the best policies to address these issues.

This Committee has examined concentration issues in previous hearings. The competitive implications of consolidation and concentration in production agriculture and agribusiness are numerous. Situations of monopoly or monopsony can result from reduction in the number of market participants or an increase in the market share of the participants. Unique among Federal statutes that are within the purview of the Department of Agriculture, the Packers and Stockyards Act provides the Secretary with legal authorities to take actions against activities by packers in interstate commerce that have the effect of restraining commerce or creating a monopoly in commerce.

The USDA has restructured the Grain Inspection, Packers and Stockyards Administration to strengthen enforcement of anti-competitive practices and improve the agency's ability to enforce the provisions of the Packers and Stockyards Act. Today the Committee will examine the present structure and functions of the Grain Inspection, Packers and Stockyards Administration. This marriage of two previously independent agencies occurred in 1994, intended to secure a productive and competitive global marketplace for U.S. agricultural products.

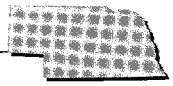
I welcome Mr. Michael Dunn, Under Secretary for Marketing and Regulatory Programs, and Mr. James Baker, Administrator of the Grain Inspection, Packers and Stockyards Administration. I have asked Mr. Baker to provide testimony addressing the challenges facing GIPSA. Under Secretary Dunn may offer additional remarks. I take this opportunity to thank Mr. Baker for coming to my home state of Indiana, in order to receive input from Hoosiers farmers regarding concentration and consolidation. I also welcome Mr. David Shipman, Deputy Administrator of the Federal Grain Inspection Program, who is present to respond to questions the Committee may have regarding his program.

I am pleased that Dr. Philip Paarlberg and Dr. Kenneth Foster from Purdue University are with us today. They will review the findings in their recent paper titled "Structural Change and Market Performance in Agriculture: Critical Issues and Concerns about Concentration in the Pork Industry."

Today's third panel contains producer representatives who will provide commentary on the

UNITED STATES SENATOR • NEBRASKA

CHUCK HAGEL



Tuesday, February 1, 2000

Opening Statement of Senator Chuck Hagel
Senate Agriculture Committee
Hearing on Agribusiness Concentration

Mr. Chairman. Thank you for holding this important hearing today. It is appropriate for Congress to examine the complex issue of consolidation in agribusiness.

I am a cosponsor of your bill, S.1984, that would create a position in the U.S. Department of Justice Antitrust Division to focus on enforcing antitrust laws relating to agribusiness mergers.

With the rapid increase in consolidations within the agriculture industry, it is important that we create a special position in the Justice Department to specifically focus on enforcing antitrust laws in this area. I do not support arbitrarily blocking agribusiness mergers, but we must make sure that the changes occurring in this industry do not result in concentrations of power or deceptive business practices that unfairly impact our agricultural producers.

I was pleased to learn of the Justice Department's recent decision to create this new position. The addition of the agriculture position within the Justice Department is a significant step toward recognizing the unique features of the agriculture industry and the remarkable structural changes that are taking place. However, I would encourage my colleagues to pass this legislation to ensure the position endures future Administrations.

Our grain and livestock producers deserve clear and direct answers. As producers, they are facing the lowest prices in years for their products, yet retail prices have remained fairly stable. The margin between the farm and the table is growing wider. Why? We need to get a better understanding of this disparity. Members of Congress need to have a clearer picture of the impact and the consequences of the rapid increase in market concentration in agriculture.

These questions must be answered in a thorough, deliberative manner in order to construct a sound agriculture policy--one that ensures the continued productivity of our nation's farmers. I hope this hearing will begin the process of answering these questions and help provide solutions to these challenges.

Testimony of
James R. Baker, Administrator
Grain Inspection, Packers and Stockyards Administration
before the
Senate Agriculture, Nutrition, and Forestry Committee
February 1, 2000; 9:00 AM

Good morning, it's an honor to be here today to review the current and future operations of the Grain Inspection, Packers and Stockyards Administration (GIPSA). Our mission is to facilitate the marketing of livestock, poultry, meat, cereals, oilseeds, and related agricultural products and to promote fair and competitive trading practices for the overall benefit of consumers and all segments of American agriculture. We fulfill this mission through two programs: our grain inspection program, commonly referred to as the Federal Grain Inspection Service, or FGIS, and our Packers and Stockyards, or P&S, Program.

Industry consolidation, technological advances and global trade have altered and will continue to reshape the agricultural landscape and to influence the job we have to do at GIPSA. Our grain inspection program must keep pace with the changing needs of the grain industry, especially in terms of inspection timeliness and the capability to measure new diverse quality attributes. Today's grain market handles a greater diversity of grain quality than ever before and must do so efficiently and productively for American agriculture to remain competitive in the global market. Next-day inspection services that met the markets needs just a few years ago now must be provided in minutes if unit trains, barges, and vessels are to be loaded efficiently.

Likewise, the structural changes in the livestock industry have complicated the job of our Packers and Stockyards Program. High concentration, forward sales agreements, production contracts, and vertical integration have raised major concerns about competition and trade practices in livestock and procurement by meat packers and poultry processors. Concentration in the meat packing industry is relatively high and has been growing. The four leading packers' share of steer and heifer slaughter increased from 36 percent in 1980 to 81 percent in 1998. Concentration in hog slaughter is not as high, but also is on the rise, increasing from 34 percent in 1980 to 56 percent in 1998. In addition, both the slaughter and production of livestock have become more concentrated into relatively narrow geographic regions.

These changes are impacting how we do business today and how we will operate in the future. We are ready to meet these and all other challenges that may arise. I'd like to take this opportunity to discuss in more detail the current status of our grain and P&S programs, and to give you an idea of the major issues each program is addressing.

GIPSA's Grain Inspection Program

GIPSA's grain inspection program administers the United States Grain Standards Act, which established uniform, national grain inspection and weighing programs. The Act generally requires that export grain be inspected and weighed; prohibits deceptive practices and criminal acts with respect to the inspection and weighing of grain; and provides penalties for violations. Under the Act, GIPSA establishes the official grading standards for grain, develops standard testing methodologies to measure grain quality and quantity, and provides for the impartial application of the grades and standards through the official grain inspection and weighing system, a unique network of Federal, State and private inspection agencies. Briefly, the U.S. Grain Standards Act provides for the mandatory inspection and weighing of all export grain and the voluntary inspection and weighing of grain moving in domestic commerce. Services under the Act are performed on a fee basis for both export and domestic grain shipments. GIPSA's grain program has both service and regulatory roles, It was founded to provide impartial, accurate quality and quantity measurements to create an environment that promotes fairness and efficiency.

GIPSA also administers and enforces certain inspection and standardization activities related to rice, pulses, lentils, and processed grain products such as flour and corn meal, as well as other agricultural commodities under the Agricultural Marketing Act of 1946 (AMA). Services under the AMA are performed upon request on a fee basis for both domestic and export shipments by either GIPSA employees or individual contractors, or through cooperative agreements with States.

The grain program is comprised of 555 full-time, permanent employees and 74 part-time, intermittent, or other employees located at 2 headquarters units, 13 field offices, 2 Federal/State offices, and 6 suboffices. FGIS has headquarters units in both Washington, DC, and Kansas City, MO. Field offices are located in Stuttgart, AR; Sacramento, CA; Moscow, ID; Cedar Rapids, IA; Wichita, KS; New Orleans, LA; Baltimore, MD; Minneapolis, MN; Kansas City, MO; Grand Forks, ND; Portland, OR; League City, TX; Toledo, OH; and Olympia, WA; thus ensuring the availability of official inspection and weighing services anywhere in the United States. FGIS personnel also are located in eastern Canada to provide inspection of U.S. grain at Canadian ports.

Mandatory inspection and weighing services are provided by GIPSA on a fee basis at 37 export elevators. Under a cooperative agreement with GIPSA, the Canadian Grain Commission provides official services, with GIPSA oversight, at 6 locations in Canada exporting U.S. grain. Eight delegated States provide official services at an additional 19 export elevators under GIPSA oversight.

Official inspection and weighing of U.S. grain in domestic commerce are performed upon request and require payment of a fee by the applicant for services. Domestic inspection and weighing services are provided by 59 designated agencies that employ personnel licensed by GIPSA to provide such services in accordance with regulations and instructions.

Reauthorization

On September 30, of this year, several provisions of the U.S. Grain Standards Act will expire. Specifically, as of September 30, 2000, the following sections of the Act will sunset: the authority to collect and invest user fees from official agencies for supervising their performance of official inspection services (7 USC 79 (j)(4)); the authority to collect fees to perform original weighing services and to collect user fees from official agencies for supervising their performance of official weighing services (7 USC 79a(l)(3)); a 40% cap for total administrative and supervisory costs (7 USC 79d); appropriations for standardization, compliance, and international monitoring activities (7 USC 87h); and authority for the Grain Inspection Advisory Committee (7 USC 87j(e)).

We believe it is in the best interest of American agriculture and consumers that these provisions are reauthorized. Consequently, GIPSA will be pursuing legislative reauthorization of these provisions of the Act for a period of 10 years. In addition, GIPSA will be seeking several new legislative authorities. First, while GIPSA seeks to maintain official agencies' geographic boundaries, the Agency is requesting authority to allow for exceptions by regulation (similar to existing pilot programs (7 USC 79(f)(2); 7 USC 79 a(i)). GIPSA also will be seeking to prohibit adding bleach, vanilla, cinnamon, etc. to any grain to disguise its quality (7 USC 87(e)(1)). This practice is already prohibited on officially-inspected grain. This new prohibition would, like the existing ban on adding water to grain, extend to all grain. Third, GIPSA will be seeking to eliminate the export sampling procedure requirement to obtain samples after final elevation (7 USC 77(a)(1)). This would provide more flexibility to respond to new marketing trends. Finally, GIPSA will be seeking authority to eliminate mandatory annual testing of official equipment (7 USC 79b(a)). Annual testing simply is not necessary or appropriate for some types of equipment.

Given that overview, I'd like to take a few moments to highlight the grain program's initiatives in four areas: efficiency enhancements; biotechnology; grain cleaning; and grain contracting.

Efficiency Enhancements

The grain program has made a number of enhancements to its operations and structure to improve the efficiency and productivity, not only of the inspection and weighing process and GIPSA's service delivery, but, more importantly, to the actual handling and marketing of grain.

Structurally, GIPSA has, over the years, continuously restructured to optimize its staffing levels and organization. Since 1994, the grain program reduced staffing levels by 8 percent and streamlined its field structure from 31 to 21 offices, thereby allowing for more flexible staff utilization and more consistent policy implementation. Our Commodity Testing Laboratory, formerly in Beltsville, Maryland, was merged into our Technical Center in Kansas City, MO. The Technical Center is now a model of how

streamlining and cross-functional teams can result in cost efficiencies and a sharpened customer service focus.

We also are reengineering to provide more efficient and effective programs and services. We reengineered our quality assurance program, already known worldwide for ensuring consistent and accurate inspection and weighing results. By automating to a PC-driven system and decentralizing the process to the local level, our reengineered quality assurance program provides for proactive problem solving and immediate quality control feedback. Automation is also the key to improving our inspection services. To integrate our export inspection process with the export industry's technological advances, GIPSA is automating the export inspection statistical shiploading plan, also known as Cu-Sum Plan. Automating Cu-Sum allows for direct data sharing with our export grain customers, thereby eliminating manual data entry and reducing administrative costs both for GIPSA and our customers. We are working closely with export elevators to automate their scales and material systems to official requirements. This automation reduces official oversight personnel, which produces a considerable cost savings for our customers, and provides for superior supervision and greatly improved efficiency for GIPSA. Five export elevators are operating approved systems; 6 more are in the process of automating. To improve the efficiency and productivity of U.S. grain handling, GIPSA established a public/private partnership to automate inspection processes. This effort reduced the agency's operating costs and improved the speed, productivity, and efficiency of export operations - essential factors in today's competitive global market. A prototype system currently is being installed at an export elevator in Destrehan, Louisiana. These are only some of the ways that GIPSA is seeking to enhance the efficiency of our operations. Future technological advances and customer needs will drive even further improvements.

GIPSA's service delivery costs decreased from $0.27 per metric ton in fiscal year 1994 to $0.21 per metric ton in fiscal year 1999, saving American agriculture over $5 million in fiscal year 1999 alone. These savings in inspection service costs pale in comparison to the savings achieved by the industry thorough improved productivity. GIPSA is proud to be a partner with the industry in realizing that productivity enhancement. Last year, at a single facility in Iowa, GIPSA fostered a unique and unprecedented cooperative partnership to provide service and made rules more flexible in order to implement a new, on-site rapid inspection program that saved one customer more than $250,000 per year.

Meeting our customers needs doesn't stop with efficiency enhancements. It also means we must be ready to meet new and emerging market needs in many areas such as biotechnology, grain cleaning, and grain contracting.

Biotechnology Reference Laboratory

Biotechnology is diversifying grain and oilseed quality, and has the potential to create new market opportunities for America's producers, small and large, as end users seek suppliers of unique quality attributes. While GIPSA, under the United States Grain Standards Act (USGSA), has no authority to approve or release biotech crops, we do

have responsibility to facilitate the fair and orderly marketing of grain and grain products, many of which will be bioengineered. To this end, GIPSA will continue to assess the market's needs; meet those needs by providing the standardized testing technology that measures new and enhanced value products; and provide that information to all in the U.S. grain marketing system, from producer to end user.

As we discussed earlier, GIPSA is responsible for establishing the official U.S. standards for grain under the U.S. Grain Standards Act. These standards are used every day by sellers and buyers to communicate the type and quality of cereals, pulses, and legumes bought and sold. Biotechnology is affecting this program in two fundamental ways: (1) increased market opposition to bioengineered crops has created a need for standardization of reliable testing methodologies to distinguish bioengineered from non-engineered crops; and (2) an anticipated increase of new value-enhanced traits, whether produced by conventional or non-conventional means, will create an expanded need for standardized testing methodologies to measure the enhanced quality attributes. Without standardized testing methodologies and an agreed-upon means to communicate the results, market risk will increase and the true value of future crops will be less transparent.

To meet the market's need for impartial, professional verification of biotechnology testing technologies, GIPSA will begin to establish a biotech reference laboratory during this fiscal year 2000 in Kansas City, Missouri. The laboratory will evaluate and verify analytical procedures used to detect and quantify biotechnology traits in grains and oilseeds, and establish sampling procedures for use in testing genetically enhanced grains and oilseeds. GIPSA will implement the standardized sampling and testing methods through the official inspection and weighing program.

The reference laboratory will meet a market need to ensure reliability of biotech crop detection methods and to facilitate information exchange, which, in turn, will decrease transaction costs and increase overall market efficiency. The lab is scheduled to open in time for the 2000 soybean and corn crop year.

GIPSA also plans to increase its ability to measure enhanced quality attributes, whether produced by biotechnology or traditional breeding methods. Analytical tests required to assure the presence or specific content of a value trait are essential to ensure the supplier (i.e., farmer, cooperative, grain facility) receives the financial benefits derived from producing grain with value-added traits. These quality tests, however, may not adapt well to field analysis and may be too costly for frequent verification analysis. As an alternative to frequent testing for value traits, GIPSA will also evaluate procedures that would ensure the preservation of a specific quality trait from farm to end-user. Industry participants adhering to the procedures, based on a GIPSA audit, would be certified as meeting the specified quality attributes.

GIPSA has historically standardized numerous analytical methods to facilitate grain marketing. For example, GIPSA standardized the testing of various mycotoxins in grain by evaluating and approving commercially available test kits that measure the mycotoxin

content. Grain markets rely on GIPSA as an unbiased entity to fulfill this important role in facilitating grain marketing.

Once we have more standardized detection methods for bioengineered grains and oilseeds, American agriculture, and our government, will be in better positions to open markets for our grains and oilseeds.

Another issue impacting markets for America's grain is grain cleaning.

Grain Cleaning

Importers of U.S. wheat frequently rank cleanliness as their number one complaint about our wheat quality. Canada and Australia, major competitors for U.S. wheat exports, have incorporated a cleaning strategy in their marketing system which results in lower dockage (levels of 0.1 to 0.2 percent versus 0.7 percent on average for U.S. wheat). Foreign material and shrunken and broken kernels are about 50 percent less than in U.S. wheat. Over the past 10 years, several importers of U.S. wheat have revised their contract specifications to reduce the allowable level of dockage in their purchases. Since 1990, the average dockage in U.S. wheat shipped to Japan has been reduced from 0.7 to 0.4 percent; to South Korea, from 0.7 to 0.5 percent; and to Taiwan, from 0.6 to 0.4 percent. Taiwan has more stringent dockage specifications than any other importer of U.S. wheat; they specify maximum 0.5 percent dockage, with an accelerating discount scale above 0.1 percent.

Effective this January, Japan imposed a maximum 0.4 percent dockage specification and announced intentions to reduce the limit to 0.3 percent in the year 2002. Korea will impose a maximum 0.5 percent limit in April 2000. Several other important U.S wheat customers, including Egypt, the Philippines, and Venezuela, also have reduced their dockage specifications. This trend may continue as smaller volume buyers, historically not known for quality consciousness, continue to privatize and impose stricter specifications.

GIPSA contracted with USDA's Economic Research Service to examine the cost and benefits of cleaning <u>all</u> U.S. wheat exports. The study concluded that mandatory cleaning of all U.S. exports is not economical, but that mandatory cleaning could potentially increase U.S. exports by up to 2 percent. ERS also concluded that targeted cleaning for quality conscious markets could have positive economic results, especially in the event of increased privatization among importers.

Since the ERS study, privatization of import markets has accelerated, increasing the importance of wheat quality as a purchasing criterion. While less than 25 percent of the world wheat trade was conducted by private importers just 10 years ago, this year private buyers will purchase 55 to 60 percent of wheat imports and will account for at least 25 million tons more trade than a decade ago.

Last November, the Commodity Credit Corporation solicited comment as to whether USDA should finance the installation of grain cleaning systems at wheat export elevators in the U.S. On January 28, USDA conducted a public hearing to solicit comment on improving the quality and competitiveness of U.S. wheat exports by financing grain cleaning systems at export elevators. USDA is considering financing grain cleaning systems.

As discussed earlier, the market relies on the Official U.S. Standards for Grain as a common language to describe the physical and biological condition of grain to facilitate trade. In terms of cleanliness, the quality criteria in the U.S. wheat standards primarily address three areas: impurities and unmillable material (dockage, foreign material, and shrunken/broken kernels); imperfections (defects and damaged kernels); and wholesomeness (insect infestation, toxic seeds or substances, and odor).

Dockage and foreign material are different, and are calculated independently. Dockage includes extraneous material larger and smaller than wheat separated mechanically by sieves and riddles, and lightweight material separated by aspiration. Dockage is expressed as a percentage of weight of the original sample but is not controlled by maximum limits in the standards. Foreign material is any non-wheat material (mostly non-wheat grains and other seeds) remaining in the sample after the removal of dockage and shrunken and broken kernels. The wheat standards define maximum limits of foreign material for each numerical grade.

Currently, there are no limits for dockage in any grade of wheat in the U.S. Standards, unlike other grading factors such as test weight, foreign material, and damaged kernels. Dockage is determined on every sample of wheat graded, but maximum or average dockage limits are determined by buyers and sellers in their sales contract.

Grain Contracting

While our export market has always relied upon contracts to transact grain sales, it is only recently that we're seeing growing use of contracting in the domestic market. Farmers are increasingly diversifying their production to capitalize on opportunities to enter niche markets for high value grains and oilseeds. As they do that, many are electing to enter contracts for certain products -- such high oil, waxy, or nutritionally dense corns, hard white wheat, or NuSun sunflowers -- to ensure they have customers for their product.

While GIPSA doesn't approve or monitor grain contracts, we do have a vitally important role to play. We will, as always, standardize testing to help producers ensure that they're getting a fair price for their product. Standardized testing methods for quality traits not only provide buyers with simple ways to describe the quality of grain they wish to buy, they also give sellers (i.e., farmers) the ability to measure the quality and know they value of their grain.

For example, under a typical high oil corn contract, the premium paid to the farmer is based on a test performed by the buyer. To ensure fairness to all involved, the typical

contract under which high oil corn is produced also allows the farmer to have GIPSA measure the oil content. In other words, if the farmer questions the buyers' oil results, he/she, working with the buyer, can obtain a representative sample of the corn and send it GIPSA for testing. Final settlement is then based on the GIPSA result. There is no greater testament to the accuracy of our testing and our overall integrity in the eyes of the market.

GIPSA's goal is to ensure that standardized testing methods are available to the marketplace for the new generation of high value crops that will be brought to the market in the future. These methods will ensure that producers, as well as buyers, have the accurate quality measurements they need to effectively and equitably market their products.

Ensuring market fairness also is a priority for our Packers and Stockyards Programs.

Packers and Stockyards Program

GIPSA's Packers and Stockyards (P&S) program addresses issues relating to competition, financial protection, and trade practices in the livestock, meatpacking, and poultry industries under the authority of the Packers and Stockyards Act of 1921, as amended. The P&S Act makes it unlawful for a regulated firm to engage in unfair, unjustly discriminatory, or deceptive practices. Manipulation of prices, market allocation, and the restraint of commerce are violations of the Act, as well.

Under the Act, GIPSA investigates alleged violations of the Act and prosecutes violations either directly through administrative actions or through injunctive relief or collection of civil penalties litigated in the District Courts by the Department of Justice.

The P&S program has three principal areas of responsibility: financial protection, fair trade practice enforcement, and promotion of competitive marketing conditions.

To ensure that producers are paid promptly and fully, P&S requires the registration and bonding of each marketing agency and dealer, and, since 1976, also requires that packers be bonded. Since the 1976 amendment to the P&S Act established the packer trust, livestock sellers have been paid more than $53.8 million under the statutory trust provisions. Similarly, the P&S Act was amended in 1988 to include a statutory trust provision for live poultry dealers similar to the packer trust, thereby giving payment protection to live poultry growers and sellers. Since then, live poultry producers have been paid $7.3 million under these statutory trust provisions.

To guard against unfair trade practices in the sale of livestock, meat, and poultry products and services, P&S regularly investigates false weighing allegations; contract poultry arrangements that may violate the P&S Act; fraudulent marketing practices, such as weight and price manipulation, and misrepresentation of livestock's origin and health;

and allegations of fraud, including collusion between or among dealers, order buyers, market agencies, or packer employees engaging in payoffs and kickback schemes.

To guard against anticompetitive business practices, P&S conducts broad investigations both of industry practices and individual firms' behavior. We investigate allegations of failure to actively compete in the procurement of livestock, territorial allocation, turn-taking, and packers' use of marketing arrangements and packer-owned supplies to influence spot market prices.

P&S recently completed a major restructuring and restaffing to strengthen its investigations of anticompetitive behavior and increase its efficiency and effectiveness in enforcing the trade practice and payment protection provisions of the P&S Act. P&S' 11 field offices were consolidated recently into 3 regional offices in Denver, CO (cattle and sheep); Des Moines, IA (hogs); and Atlanta, GA (poultry). This resulted in the location of significantly larger staffs near the concentrations of beef, pork, and poultry production and slaughter. We have added staff with economic, statistical, and legal expertise to strengthen competiveness investigations. We are pleased that Congress provided additional funds last year to enable GIPSA to make these improvements.

USDA has undertaken a number of initiatives to investigate livestock and poultry procurement practices, strengthen oversight and provide more information to producers:

1. **Rapid Response Teams**–USDA dispatched rapid response teams to South Dakota and Missouri in July and September, respectively, to respond to producers' concerns and to ensure adherence to the P&S Act in light of new price discrimination laws enacted in those States that influenced the procurement practices of packers in the States.

2. **Hog Contract Library and Monthly Contract Use Reporting**–As called for by the Mandatory Livestock Reporting Act of 1999, USDA is establishing a library of contracts offered by hog packers to producers for the purchase of hogs. The Department will also collect and summarize information on the numbers of hogs committed by contract for upcoming 6 and 12 month periods. Information on the types of contracts and projected hog numbers will be released monthly.

3. **Excel Complaint**–USDA filed a formal complaint against Excel alleging that the firm violated the P&S Act by failing to disclose to producers a change in the calculation of lean percent for hogs purchased on a carcass merit basis, and that, as a result of this change in formula, Excel paid lower prices for a majority of hogs bought..

4. **Farmland Complaint**–USDA filed a formal complaint against Farmland National Beef Packing Company, alleging that the company violated the P&S Act by changing its business practices by failing to make bids or purchase cattle at Callicrate Cattle Company Feedyard, St. Francis, Kansas, after an article critical

of Farmland written by Callicrate Feedyard's sales manager was published in a livestock journal.

5. **Texas Fed-Cattle Investigation**–GIPSA conducted a broad investigation of fed steer and heifer procurement in the Texas Panhandle covering the 1995-96 period. The investigation examined procurement areas, procurement methods, and pricing methods. GIPSA's investigation found substantial variation in the use of methods of cattle procurement. It found in the econometric analysis performed under cooperative agreement with university researchers that the statistical association found in other studies - an increase in non-spot purchases was associated with lower spot prices - was found in the Texas data as well. The estimated statistical relationships appear to suggest that reducing non-spot purchases or increasing spot purchases could have a positive effect on spot price. However, the researchers note with regard to this suggestion that a statistical association does not prove causation. In addition, they caution that the policy relevance of this empirical regularity depends on the nature of the economic mechanism responsible for generating it. To illustrate their point, they suggest that the actions of feedyard managers who sell cattle through non-spot arrangements could contribute to the finding that a greater volume of non-spot purchases was associated with lower prices. This is because feedyard managers generally control when cattle are delivered under marketing agreements and because non-spot cattle are priced the week before delivery.

6. **Investigation of Hog Procurement Contracts** – GIPSA is reviewing the terms of hog procurement contracts to ensure that individual contracts comply with the P&S Act.

7. **Contract Poultry Settlements**–GIPSA is engaged in major investigations to determine whether contract poultry grower settlements are fair and to ensure that growers are not being settled in an unjustly discriminatory manner. Extensive grower settlement information from several of the largest poultry integrators is being analyzed during these investigations.

8. **Poultry ANPR**–An Advance Notice of Proposed Rulemaking (ANPR) relative to contract production of poultry was published in the *Federal Register*. Comments were received from all segments of the poultry industry on the need for additional rulemaking in the areas of: 1) feed weighing and delivery; 2) live bird weighing operations; and 3) grower payment based on a comparison of grower's production costs. Over 3,400 comments were received in response to the ANPR. Regulations relative to feed weighing and delivery have been prepared and are in the clearance process.

9. **Cooperative Research Agreements on Competition in Livestock and Poultry**–GIPSA recently entered into cooperative agreements with researchers at universities across the Nation to address issues related to concentration. These agreements include: *A New Direction for Assessing Market Power in the Beef*

Packing Industry, conducted by Lynn Hunnicutt, DeeVon Bailey, and Quinn Weninger, Department of Economics, Utah State University; *An Analysis of the Effects of Captive Supply in Fed Cattle Marketing in the Texas Panhandle*, conducted by David Bessler, Department of Agricultural Economics, Texas Agricultural Experiment Station (Texas A&M University); *Economic Effects of Regulating Broiler Contracts*, conducted by Tomislav Vukina, Department of Agricultural and Resource Economics, North Carolina Agricultural Research Service (North Carolina State University); *The Market for Poultry Grower Services: Dimensions and Market Power Exertion*, conducted by Victoria Salin and Alan Love, Department of Agricultural Economics, Texas Agricultural Experiment Station (Texas A&M University); and *Competitive Bidding in Simulated Auction Markets*, conducted by Dale J. Menkhaus and Owen R. Phillips, Department of Agricultural and Applied Economics, University of Wyoming.

Now I would like to discuss legislative initiatives that would enhance GIPSA's ability to protect producers and growers and to take action against unfair trade practices or anticompetitive practices.

The first legislative initiative would amend the P&S Act to establish a statutory trust for the benefit of sellers of livestock to dealers and market agencies buying on commission. USDA has drafted and submitted to Congress a bill for review.

Market agencies selling on commission have long been required to handle funds received from the sale of consignor's livestock as trust funds and to use a special bank account designated "Custodial Account for Shippers Proceeds." The Act was amended in 1976 to provide for statutory trusts to cover livestock sales to meat packers in the event of a business failure or other instances of packers' failure to make payment. The Act was amended in 1988 to provide statutory trust protection to poultry producers.

Dealer failures represent a significant amount of unrecovered losses in the livestock marketing chain. For fiscal years 1994-98, dealer failures averaged 14 per year. Amounts owed to livestock sellers averaged $3.1 million per year. Of this amount, producers only recovered about 25 percent of the amount owed. During the same period, an average of 9 packer failures per year resulted in an average annual payout of $1,759,243 from the packer trust. A dealer trust for cash sellers of livestock would minimize the losses suffered by livestock producers because of dealer failures to pay.

The second legislative initiative would amend the Packers and Stockyards Act to grant USDA administrative enforcement authority over contract poultry production. This proposed legislation is contained in the Poultry Farmers' Protection Act of 1999 (H.R. 2829), introduced by Representatives Kaptur and Emerson on September 9, 1999.

Under Section 202 of the Act, packers and live poultry dealers are prohibited from various unfair, deceptive or unjustly discriminatory practices. A live poultry dealer is

defined as any person engaged in the business of obtaining live poultry by purchase or under a poultry growing arrangement for the purpose of slaughter or for sale to others for slaughter. Enforcement of Section 202 against a packer is accomplished through an administrative proceeding before an Administrative Law Judge. Enforcement against a live poultry dealer can only be accomplished through referral to a U.S. Attorney's office and filing in Federal Court. This is because Section 203 of the Act, which authorizes administrative enforcement, provides for actions against "packers" and not "live poultry dealers." We believe that regulation of the activities of live poultry dealers would be more efficient if the Act were amended to provide for administrative enforcement authority.

GIPSA continues to evaluate potential regulatory and legislative actions, and we have a number of investigations currently underway. We have done much to move the P&S program forward and will continue down this path to ensure fair and competitive markets for America's livestock, meatpacking, and poultry industries.

Conclusion

The United States is the world's leader in food and fiber production. We at GIPSA are working to help the Nation maintain that leadership by providing the information, services, and protection that American agriculture needs to flourish. Open, competitive markets have been and will continue to be essential to the Nation's overall well being.

I appreciate the opportunity to address the Committee and I will be happy to respond to your questions.

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Statement of Senator Peter G. Fitzgerald
Agriculture Committee Hearing
Concentration in Agribusiness
Tuesday, February 1, 2000

Good morning. Mr. Chairman, I appreciate you scheduling this hearing and thank the witnesses for joining us today. First, I would like to welcome two of my constituents who will be testifying today. Ron Warfield from Gibson City, Illinois serves as the Illinois Farm Bureau President and Mike Clark of Homer, Illinois is active in the National Corn Growers Association.

Market concentration in the agricultural industry is an issue that is receiving significant attention in farm country. With the agricultural economy in a severe slump for many commodities, the level of volume on this issue has only increased. While the problems facing our farmers are primarily an issue of supply outpacing demand, we need to ask some tough questions about the degree of concentration within the agricultural industry.

Clearly concentration in agriculture continues to increase, the question is "how much is too much?" I encourage the Packers and Stockyards Administration and the Justice Department to be diligent and monitor this situation closely. If they find collusion or price fixing, it is illegal under our current laws and violators should be punished.

Some farm organizations have argued that current law in this area is not sufficient. These contentions should not be quickly dismissed nor accepted blindly. Thus, in May of last year, Senator Grassley and I sent a letter to Attorney General Reno asking her to

expedite her review of current anti-trust laws to determine if new legislation was needed in this area. With commodity prices at near record lows, we must ensure that agricultural markets are competitive and open to family farmers. I was encouraged to hear that the Senate Judiciary Committee will also hold hearings on this important issue in the near future.

I support providing agricultural producers the best, most timely information possible. Producers can use this information to make better marketing decisions and hopefully capture more value at the farm level. Last year, this committee passed mandatory price reporting legislation to do just that. I am interested to hear today how USDA implementation of this program is moving forward.

Additionally, I am pleased to announce today that I will be joining Chairman Lugar and Ranking Member Harkin as a co-sponsor of S. 1984. This legislation establishes an agricultural anti-trust specialist within the Justice Department. I understand that the Justice Department has recently appointed such a person. However, S. 1984 is still needed to ensure that this position remains permanent.

Finally, I support the formation of agricultural cooperatives as an innovative way for farmers to retain more of the food dollar at the farm level. Farmers can empower themselves in an increasingly concentrated environment through involvement further up the food marketing chain. Agricultural producers, from family farms to agri-businesses, must be willing to work together to ensure the survival of America's farms and to address the growing world population.

I look forward to today's testimony. Thank you, Mr. Chairman.

Structural Change and Market Performance in Agriculture:

Critical Issues and Concerns about Concentration in the Pork Industry

Testimony of

Philip Paarlberg, Associate Professor, Purdue University

before the Senate Committee on Agriculture, Nutrition, and Forestry

February 1, 2000

Chairman Lugar and Members of the Committee:

The U.S. agricultural industry is in the midst of major structural change. Production is changing from an industry dominated by family-based, small-scale, relatively independent firms to one of larger firms that are more tightly aligned. The sector is becoming more industrialized, more specialized, more integrated, and the pace of change is increasing.

Evidence of increased concentration in hog slaughter

Like many industries, the hog slaughter industry is characterized by a small number of firms producing most of the pork and a fringe group consisting of a large number of small slaughtering firms contributing little to total pork supply. Measures of market concentration suggest that the hog slaughter (packing) industry has become significantly more concentrated since 1985. Concentration indexes for the top 4 and 8 firms have risen. In 1985, the 4-firm concentration index was 32.2 and the 8-firm index was 50.8. By 1997, the indexes had risen to 54.3 and 75.7. Traditional classification would label an industry with these concentration indexes as a moderately concentrated industry. Another measure of industry concentration is the Herfindahl-Hirschman (HH) index which is the sum of the squared market share of all firms. This index for the hog slaughter industry has more than doubled between 1985 and 1997.

The Herfindahl-Hirschman index can be used to estimate the equivalent symmetric

number of firms in an industry. That is, if all firms in an industry were the same size, how many would there be? In the case of hog packing the symmetric firm number for 1985 is 22 which is sufficiently large enough to avoid pricing distortions. By 1997, the symmetric firm number for hog packing had fallen to 10. There is no specific value where we can say serious pricing distortions due to market power arise. However, once an industry drops to a symmetric firm number of 10, concern is warranted.

Economic implications of increased concentration

While every industry is unique, economic theory offers general conclusions about pricing under oligopoly and oligopsony (imperfect competition). One factor is the nature of interaction among firms. How does a firm expect its rivals to react when its behavior changes?

A related issue is whether the goods produced by different firms are different or alike. Product differentiation is linked to how demand changes as price changes. Firms can affect the price and rival behavior. More elasticity reduces the ability to manipulate outcomes.

International trade affects the exercise of market power. Domestic firms with market power cannot raise their prices if they face either the threat of import competition or the loss of export markets.

The cost structure of an industry affects pricing. Large fixed costs and entry barriers limit potential competition and enhance market power. Fixed capacity constrains the reaction of rival firms. Economies of scale drive unit costs lower as output rises, and can reduce firm numbers. Falling unit costs lowers output prices if the mark-up is constant, but falling firm numbers increases mark-ups on output.

Vertical relationships between input suppliers and manufacturers become critical.

Vertical integration and coordination may occur for several reasons. They can be used to exercise market power.

There is limited information on these factors for the hog packing industry. There is evidence of product differentiation, yet, the aggregate demand elasticity for pork is estimated to be high compared to other foods. The U.S. and the world pork markets appear linked. It is likely that packers have limited market power for pricing the pork. On the other hand, imports of live hogs for packers is not large relative to slaughter. This suggests an industry which sets meat output with little influence on the pork price, but with potentially substantial influence over the live hog price. The hog packing industry is perceived as having large fixed costs and economies of scale. There is evidence that increasingly large numbers of hogs move under contracts. As concentration and integration increases, problems of volatile spot markets and market foreclosure for independent growers are likely to increase.

An illustration of what may be ocuring

We constructed a model to illustrate how concentration might affect the hog price as the number of packing firms declines. Because much of the information necessary to construct an accurate model of the industry is not available, we made assumptions. It is assumed that pork is a homogenous good, and each packer sets its slaughter believing that rival packers will not change their behavior. The industry consists of identical packing firms varied from 1 to 20. Because the United States trades pork with few barriers, the model assumes the price of pork is given. Hogs are treated as non-traded which gives the packers the ability to mark down the animal price. The extent of economies of scale and vertical coordination are unknown and are excluded.

The model calculates how the mark down, or price gap, from the perfectly competitive hog price changes in response to changes in firm numbers. This mark down represents the potential market power of packers to pay less for inputs than would have been the case under perfect competition. If there are 20 firms, similar to the situation in the late 1980s, the price paid to producers for hogs is 95 percent of the perfectly competitive level. As the number of packers falls, the gap on the price paid to farmers increases. At first the gap remains small. Starting from 20 firms, reduced firm numbers does not initially lead to much larger mark downs on the competitive price. When there are 14 firms instead of 20, the hog price is 90 percent of the competitive level. Going from 14 firms to 8 firms increases the mark down from 10 percent to 18 percent. Once firm numbers drop below 5 the mark down increases sharply.

The Herfindahl-Hirschman index indicates that in 1997 the industry consists of 10 symmetric firms. The illustrative results show that the range of 8-10 equal sized firms is a critical transition between the magnitudes of the mark downs. Above 10 firms a change in firm numbers does not cause much change in the mark down. Below 8 firms, the increases in mark down accelerate. It is critical to identify where the industry lies along this relationship. In the case of the model used here, if the industry is presently at 8-10 firms, policy designed to increase firm numbers may be less critical than policy designed to maintain firm numbers. In other words, it may be that the concentration which has occurred so far has not pushed us much below competitive prices, but further concentration could have serious adverse consequences for producers.

Missing information is critical

Knowing the precise shape and location of the relationship is critical. The relationship

can only serve as an illustration because critical pieces of the puzzle are missing. Assumptions are made which may incompletely reflect the hog/pork sector. These pieces must be inserted to accurately analyze the consequences of increased packer concentration. One set of critical information covers the role of vertical coordination. Data on the numbers of hogs contracted and owned, the contract terms, and costs of packing firms is required. A weakness is limited knowledge of the extent of product differentiation and supply-use data by product. With additional data, it will be possible to narrow the uncertainty of what is occurring. Providing that analysis should be a high priority.

Summary

We are witnessing the industrialization of agriculture. The structural changes have been pronounced in the pork sector and raise important questions about competitiveness of both product and input markets.

There is evidence of increased concentration to the point where public vigilance is warranted. Concentration indexes are high and may be reaching a point where mark down pricing on hogs could be significant. It is important to have the required information and analysis as soon as possible to properly assess where we are in this respect.

Structural Change and Market Performance in Agriculture:

Critical Issues and Concerns about Concentration in the Pork Industry

Testimony of

Ken Foster, Associate Professor, Purdue University

before the Senate Committee on Agriculture, Nutrition, and Forestry

February 1, 2000

Chairman Lugar and Members of the Committee:

Dr. Paarlberg has shown that greater consolidation in the meat packing and processing industry could lead to lower live animal prices paid to farmers. Likewise, increased captured supplies, via vertical integration and/or contracting, have the potential to lower prices on average and increase the variability of prices. This is especially true for producers who are not a part of the captured supply chain. Estimates from 1999 tell us that only about 36 percent of the hogs were purchased on the spot market. However, another 44 percent were purchased on formula contracts that depend on spot markets for pricing.[1]

Packers are motivated to coordinate their supply of live animals by the large fixed costs associated with a slaughter plant, and the large transactions cost of purchasing thousands of animals on a daily basis. In order to reduce their cost per unit of wholesale meat, packers need to slaughter as many animals as possible. For modern plants, this means thousands of animals each day. The risk of "coming up short" motivates the use of company owned animals and contracted purchases to ensure that the appropriate quantity and quality of animals arrive as needed. With captured supplies, transaction costs are also reduced by not having to haggle over the price of

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[1]Source: Grimes, G., J. Lawarence, and M. Hayenga

each load of animals.

Logically, packers attempt to capture the highest quality animals via contracts and vertical alliances. This can leave the lower quality animals to establish prices in the open market. Because payment schemes for most of the packer contracted animals are based on either a spot market price or the Chicago Mercantile Futures price, substantial vertical coordination may create a downward bias in the prices received by many livestock producers.

Offsetting the consolidation and integration effects

Mitigating these downward biases in live animal prices will not be an easy task. The strongest public policy instrument is anti-trust. Clearly, breaking up the larger packers would help mitigate markdown pricing due to consolidation if it exists. However, sound economic rationale, unassociated with market power, could be motivating contracting, vertical integration, and consolidation. If the societal benefits of these rationale exceed the costs of markdown pricing then the anti-trust approach would not be justified.

It is my opinion that alternative public policies do exist that could offset the price impacts of these business structures without completely foregoing their benefits. The focus of these policies would be on increasing the bargaining power of pork producers. Unfortunately, the livestock producing community has little experience and expertise in using these alternatives and will likely need public policies and assistance to get them functioning.

Cooperative Production and Marketing

Cooperative production and marketing appear to be one possible way to offset the impacts of consolidation and integration in today's pork industry. Any strategy that places livestock producers in a more symmetric bargaining position with packers will make it more difficult for packers to exploit prices or contract terms. It should also be more difficult for a packer to terminate a contract or to force less favorable terms on the producer community. The packer, in need of animals to fill a daily kill, will be compelled to negotiate a more competitive price if producer power is increased.

How many high quality hogs must a single supplier (or allied group of suppliers) control in order to maintain bargaining power with a packer? At present, it appears that 300 thousand to 500 thousand head per year, or approximately the single day double-shift kill for a moderate sized slaughter plant each week would be sufficient. This is a large number of animals and would require a sizable network of today's large independent producers. Forming such networks or cooperatives must be nurtured by public policy. Our research at Purdue has demonstrated that there are a variety of ways to structure these entities that may also allow the producers to capture cost reductions and gain access to new (and possibly proprietary) technologies that individual farms would not be capable of obtaining by themselves.

Tax incentives or deductions for members of production and marketing networks, corporations, cooperatives and alliances could provide incentives not only for producers to enter such arrangements, but such policies could also be fashioned to provide disincentives for producers to break away from the group in an effort to capture short term gains as a "free rider". Current exemption from anti-trust constraints provides some benefit for cooperative formation.

However, undercapitalization is the most common cause of failure among new cooperative ventures. A serious commitment of technical and financial support above that currently available will be needed to develop and encourage new production systems and marketing strategies that facilitate greater bargaining power for producers.

The approach needed by such groups is fundamentally different from the traditional livestock marketing cooperatives of the past. In the past, farmers independently produced the animal type of their choice and marketed them on the day of their choice to various markets. If the cooperative alliances of the future are to increase the bargaining power of producers, then the production systems of the cooperating farmers must be coordinated. Coordinated production will allow the group to provide a steady supply of hogs of uniform quality to a single packer. This supply chain must be closely managed to deliver a large number of animals on a daily basis because fluctuation in supply is not attractive to a packer and reduces producer leverage. Managing the supply chain in this way will take innovative production practices that may require greater specialization of activities by farm and standardization of mating systems, feeding strategies, genetics and so forth.

Marketing Orders

Marketing orders provide another possible policy avenue. Marketing orders are used in several agricultural markets where lack of producer bargaining power is a concern. These orders may set base prices at a particular location with premiums and discounts for other locales and involve pooling of all marketings in a given locale. Typically, they also establish quantity and quality restrictions.

If such a marketing orders were adopted for pork, it would be essential to incorporate quality premiums. Otherwise, there would be little incentive to produce high quality animals. The resulting lack of quality hogs would encourage packers to increase vertical integration and effectively exclude independent producers from the market. Furthermore, some of my own research has found that a market failure may occur if a geographical discount structure is not market driven[2]. This market failure may lead to a geographical distribution of production that is not socially optimal.

Summary

In summary, two major policy options are anti-trust activity on the one hand and nurturing increased market power of pork producers on the other. With current knowledge, we cannot recommend breaking up existing packer concentration. Such actions can be extremely contentious, and may be contrary to society's best interest. However, public policy can assist producers in gaining countervailing market power. This can happen by encouraging the formation and survival of highly structured cooperative production and marketing systems. However, many of today's independent pork producers are not familiar with these new strategies and public assistance may be necessary to get them off the ground. Finally, caution should be exercised against blanket condemnation of strategies adopted by packers or producers that enable them to compete successfully in an increasingly international marketplace.

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[2]Source: Foster, K. and A. Havenner. "Cointegration and Settlement of Commodity Futures Contracts," *Macroeconomic Dynamics*, 1999.

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Testimony of

John McNutt, President
National Pork Producers Council

Before the

Committee on Agriculture, Nutrition and Forestry
Unites States Senate

Concerning

The Structure and Authority of the
Grain Inspection, Packers and Stockyards Administration

Presented

February 1, 2000
Washington, DC

National Headquarters
P.O. Box 10383 • Des Moines, Iowa 50306 USA • (515) 223-2600 • FAX (515) 223-2646

The Other
White Meat.

Mr. Chairman and Members of the Committee;

My name is John McNutt. I am a pork and grain producer from Iowa City, Iowa and the president of the National Pork Producers Council (NPPC). Today, I am here representing all of America's pork producers as we examine the critical issues of market structure and performance and how these issues can be impacted positively on behalf of producers by the Grain Inspection, Packers and Stockyards Administration (GIPSA).

Let me be perfectly clear that America's pork producers expect nothing less than a fair, transparent and competitive marketplace. Nothing less will suffice to provide us and those who follow an opportunity to earn a livelihood while supplying customers worldwide delicious, wholesome, safe and affordable pork products.

Pork producers realize and appreciate that just like the policeman on the beat, GIPSA has a big job to do. Yet just like the policeman, GIPSA is what pork producers must rely on to guarantee fairness and justice. We commend and endorse its recent efforts to improve the performance of its far-ranging duties. The recent re-organization of GIPSA into species-specific offices is one such positive move. The issues faced in each species' markets and systems are quite unique and this new structure should allow GIPSA management and staff to fully develop those talents needed for each set of unique circumstances. In addition, we have found the new staff of the pork-specific office in Des Moines, Iowa to be both cooperative and responsive to issues of concern to the pork industry. We look forward to a continuing productive relationship.

But we would not be here today if there were not strong sentiment that GIPSA has not lived up to its responsibilities or, at least, many people's perception of its responsibilities. My real purpose today is to discuss problems faced by the pork industry and how the National Pork Producers Council believes GIPSA can better address them to ensure equitable treatment for producers, packers and, ultimately, consumers of pork.

The pork industry is changing at an accelerated pace. Concentration in the packing industry (as measured by the 4 firm concentration ratio) has grown from 32.2 percent in 1985 to 56.3 percent in 1998. Using the same measure, concentration in the production segment has grown from negligible levels in the early 1980s to about 18 percent following the recent acquisition of Carroll's Foods and Murphy Family Farms by Smithfield Foods. As recently as 1994, 71 percent of the hogs were sold on the spot market and only 17 percent were sold using a price formula. In 1999, these percentages had changed to 36 and 44, respectively. The trend has probably carried them further still today. This kind of change

raises serious questions about the effectiveness and efficiency of price discovery and the potential for manipulation and market power in hog markets.

Enhancing livestock market competitiveness for pork producers is a major objective for NPPC. In today's pork industry knowledge is power. Therefore, the following initiatives have been undertaken by NPPC in recent years to provide pork producers with the kind of information they need to make good business decisions. These initiatives include:

- Publication of several guides, such as "Production Contracting," "Pricing Early Weaned Pigs" and the just-completed "Guide to Marketing Contracts," a draft of which, though yet in print, I provide today for entry into the official record of this hearing.
- A voluntary packer price reporting system on the NPPC website. Farmland Foods is to be commended for their cooperation and assistance in this project. Unfortunately, they were the only packer that participated.
- The Mandatory Livestock Price Reporting Act of 1999. NPPC, along with this committee, led the effort to pass legislation that meets the needs of producers for information on spot market and contract prices. This legislation provides for a project to determine the Secretary of Agriculture's responsibilities, authorities and duties under the Packers and Stockyards Act. It also establishes a prominent role for GIPSA in providing a catalog of marketing contracts to help producers better understand what kinds of contracts are in force and available. We believe this role is very likely to raise GIPSA's visibility and stature in the eyes of producers.
- The NPPC Price Discovery Task Force, a committee of knowledgeable producers, consultants and academicians that studied a broad range of price discovery, price determination and risk management topics. This Task Force is still active and will remain so for the foreseeable future.
- NPPC's Producer Price Reporting initiative. A direct outgrowth of the Price Discovery Task Force, this initiative encourages producers to negotiate their free supplies of market hogs with more than one packer and to report the price to USDA's Livestock Market News Service. I provide a card that NPPC prepared to help producers in this effort.
- Facilitating the creation of "Pork America," a national producer-owned cooperative designed to assist producers and producer groups in marketing value-added products and thus capturing a larger percentage of the consumer dollar spent on pork.

Now, I would like to turn my attention to the topic at hand. We see the problems currently faced by GIPSA as four-fold.

1. Misunderstood Responsibility and Authority

You will likely hear testimony today that GIPSA needs more authority and the Department of Justice (DOJ) needs more resources or some combination of the two. Both may be correct. But the over-riding need is for an all-encompassing federal strategy to address the problems of agricultural markets in general and livestock markets in particular and the capability of communicating this strategy to the public.

GIPSA's authorities and responsibilities are not well understood by producers and many other pork value chain participants. Many simply expect GIPSA to do things it is not empowered to do. Others expect GIPSA to do things that it cannot do without due process. Yet others expect it to do things which, in our opinion, it does not have the resources to do. All of these add up to unmet expectations and, ultimately, disappointed constituents.

No one would propose that GIPSA carry out its duties without affording anyone his/her constitutional rights to due process, but the first and third "expectations" alluded to can be solved.

GIPSA and USDA must do a better job of educating the public about the provisions of the Packers and Stockyards Act and what it empowers GIPSA to do. Furthermore, they must help delineate GIPSA's market behavior regulatory responsibilities from the market structure and performance regulatory responsibilities of the Antitrust Division of the Department of Justice. The appointment of a Special Counsel within the Antitrust Division with responsibility for oversight and coordination of antitrust matters which affect agriculture should help clarify these responsibilities. Many call for DOJ to act "because GIPSA won't" when concentration is not within GIPSA's purview. The current investigation being conducted by the General Accounting Office (on behalf of the Senate Agriculture Committee in response to one provision of the Mandatory Livestock Price Reporting Act of 1999) may go far in accomplishing this goal.

GIPSA should have a plan to inform its constituency about its statutory responsibilities and authorities, what it can and cannot do and what other government agencies are charged to do. In addition, GIPSA must communicate clearly what it is doing and has done, in instances when it finds violations, as well as when it does not. To accomplish these tasks, GIPSA needs a dedicated communications department staffed with trained communications personnel.

2. Insufficient Resources

As was pointed out earlier, the hog market has gone from one in which virtually every hog was traded in an easily observable, public setting to one in which virtually no hogs are so traded. Information and data which was once easily gathered is now proprietary and frequently only available via subpoena. Many hogs are priced beyond the scope of negotiation through contractual relationships whose effect on the entire market is not well understood. It is likely that both of these changes require significantly more manpower to adequately monitor market conditions and discover any problems which may occur.

GIPSA personnel have no doubt increased their efficiency due to technological innovations over the past 20 years. However, like many other organizations, they may be finding there is only so much a computer can do. We believe, mainly from anecdotal evidence, that GIPSA does not have the human resources to fully accomplish its mission at the present time. Furthermore, it is our impression that GIPSA is likely to be uncompetitive in its salary and benefit offers to the highly trained professionals it needs to fulfill its mission. We urge Congress to solve this problem immediately and give GIPSA management the flexibility it needs to hire the best people. The market is tight for attorneys, economists and others knowledgeable about agriculture and the livestock industry.

It is paramount that GIPSA have the people on hand to make its presence known to both producers and packers. GIPSA's market performance monitoring must be constant, not sporadic. Market participants should be completely aware of GIPSA's presence, which must serve simultaneously as reassurance to the worried and a warning to the opportunist. This cannot be accomplished without adequate numbers of qualified, trained and, hopefully, experienced personnel.

3. New Problems, Old Methods, Insufficient Knowledge

All government agencies charged with enforcing America's antitrust laws are using economic theory and analytical tools, which were generally developed in the first half of this century. While some new econometric estimation techniques have been applied, most analytic and enforcement work still depends upon structural characteristics as indicators of firm behavior and market performance. And yet, the industries which GIPSA and DOJ regulate have changed dramatically. Do 4-firm and 8-firm concentration ratios and the Herfindahl-Hirschman Index mean the same thing they used to mean in a world with such rapid and extensive

communications systems? Should the criteria used to trigger concern and investigation be different in agriculture due to the seasonality and non-storability of its products? Answering these and related questions can probably be done only through basic, often theoretical, research.

Herein lies a quandary: Much of the basic research at universities is supported, either directly or indirectly, by the private sector. I ask you how many private firms or even foundations care much about the state of knowledge and basic research in industrial organization economic theory? Few private groups will benefit from such research but the public may collectively benefit greatly. Developing new theory and analytical methods for the investigation of antitrust violations is a perfect example of a subject area which must be supported by public research funding. And it is quite possible that a modest amount of funding will go far and accomplish more than one goal. It may both attract graduate students (who will then occupy some degree of time and talent of a major professor) and yield trained analysts for the job market. We urge Congress to fund and GIPSA and DOJ to immediately initiate a competitive research grant and research fellowship program in industrial organization and antitrust economics.

One new tool which should benefit GIPSA is the coming mandatory price reporting system. This system will provide more standardized and accurate data for GIPSA monitoring and enforcement efforts than has frequently been available in the past. Yet this system will provide only market-wide data. There still may be a need to prescribe some basic, standardized data formats for which packers must keep records in order to facilitate the monitoring, research and enforcement process.

Finally, it is important that the pork industry get more attention in GIPSA- and USDA-funded research regarding market structure and performance. We find ourselves reciting the refrain of "Not much is known for sure about the hog market but a significant amount is known about cattle markets" far too often. We need specific research to determine relevant markets for hogs, determine the effect of contracted hogs and other captive supplies and estimate the impact of vertical acquisitions which have been so newsworthy in recent months. Pork producers have real concerns about these issues, but have to rely on implications from beef industry research to make important policy and strategic decisions. It's likely inaccurate to draw such conclusions and patently unfair to ask pork producers to do so.

The last point we offer on research or investigations is this: Any pork industry research must be executed and published in a timely manner. Past delays of GIPSA investigations and reports have done much to cloud the results and invite criticism. We believe this is largely a matter of

resources and we understand that care must be taken, but a higher sense of urgency in completing necessary work is badly needed.

4. Insufficient or Under-Defined Authority

It appears to us that GIPSA and DOJ face several areas in which they have insufficient authority or in which current law is not clear enough to provide them effective marching orders. One example is the focus of antitrust legislation on monopoly power by sellers and its relative silence regarding monopsony power by buyers. Another is the need for GIPSA to test through court procedures any new interpretation of the broad prohibitions of Section 202 of the Packers and Stockyards Act. Might there be a way of spelling out a few acts which constitute *per se* violations of the act and thus save time and money in ensuring fair and competitive markets? Aren't there some specific requirements which GIPSA can employ to clearly delineate what packers must and must not do on subjects such as lean prediction equations, payment matrixes and the relationship between the two? Can't basic requirements be established to ensure that carcass information or kill sheet information is understandable and re-producible by a producer with some reasonable level of math skills? Our impression is that GIPSA does not feel it has the clear authority to answer these questions affirmatively.

The aforementioned GAO study of the Secretary's authorities, duties and responsibilities will address this topic specifically. In addition, we suggest that Congress actively seek the input of these agencies regarding items that would better enable them to do the job expected of them by the public.

Closing

In closing, the NPPC is committed to a fair, transparent and competitive marketplace. We have developed and implemented a number of initiatives to enhance the knowledge of producers and the transparency of pricing as well as competition in the marketplace. We also recognize that GIPSA must play a significant role in providing market information and oversight that pork producers have a high level of confidence in.

Mr. Chairman, thank you for holding this important oversight hearing and for giving me the opportunity to address the committee. The National Pork Producers Council stands ready to assist you in your work in any way possible.

Testimony

on behalf of the

NATIONAL CATTLEMEN'S BEEF ASSOCIATION

in regard to

Packers and Stockyards Administration Oversight

submitted to

Senate Committee on Agriculture, Nutrition and Forestry

The Honorable Richard G. Lugar, Chairman

submitted by

Rita Sharma
Williamsport, Indiana
National Cattlemen's Beef Association

February 1, 2000

Initiated in 1898, the National Cattlemen's Beef Association is the marketing organization and trade association for America's one million cattle farmers and ranchers. With offices in Denver, Chicago and Washington D.C., NCBA is a consumer-focused, producer-directed organization representing the largest segment of the nation's food and fiber industry.

Statement by Rita Sharma, Williamsport, Indiana
National Cattlemen's Beef Association
Senate Committee on Agriculture, Nutrition and Forestry
Hearing on Packers and Stockyard Administration Oversight
February 1, 2000

Thank you Chairman Lugar, Senator Harkin and Members of the Committee for holding this hearing to discuss Packers and Stockyard Administration (P&SA) oversight and other regulatory issues that concern the meat industry. NCBA commends your leadership and continuing efforts to examine the ongoing change and resulting issues and concerns of interest to cattlemen and women, and for working with us to find ways to improve our ability to more effectively market U.S. beef. I am Rita Sharma, a seedstock producer from Williamsport, Indiana and a member of the National Cattlemen's Beef Association.

NCBA encourages open and honest discussion of all issues facing the cattle industry, such as is being provided by today's hearing. Such debate is vital to the democratic policy development process -- both within NCBA and to the nation at large. NCBA has long supported mandatory reporting for export sales and shipments and for boxed beef sales prices and volumes. During the last session we worked with members and staff of this committee to improve availability of market information and enhanced competitiveness through market forces. The industry supported mandatory reporting of procurement prices and terms of trade for slaughter cattle and improved reporting of boxed beef prices, retail prices, imports and exports in a comprehensive price-reporting package. We thank you again for that initiative.

A Changing Industry:
This hearing is a continuation of an ongoing soul-searching process that is resulting from change in the livestock industry and concerns of livestock producers as they struggle to cope with change in a very competitive domestic and international marketplace. Price and volume reporting are only a piece of a larger debate over wide-ranging changes that are sweeping the livestock sector and agriculture in general. There is a broad range of opinions among beef producers about the effects of international trade agreements, packer concentration and improvements in price discovery and market reporting on the beef industry.

The structural changes taking place in the beef industry have coincided with volatility in international economies, changes in supply, a weak, but recently improving beef demand and weather-influenced volatility in feed grain and forage prices. How these factors are inter-related is the basis for heated debates, emotional arguments and general consternation by some individuals within the beef industry. Some producers have embraced new marketing techniques for their own advantage, while others believe structural changes are, at least in part, the cause of price declines during the mid to late1990s.

A vocal beef industry minority perceives that increased regulatory action is warranted. P&SA data show that the four largest packers slaughter approximately 80 percent of all steers and heifers marketed, but this percentage has not changed appreciably since 1990. NCBA policy supports close monitoring of mergers and acquisitions and enforcement of antitrust laws and regulations. Close evaluation of price movements and margins are requested to assure that price changes are the result of market signals and not the exercise of market power or illegal pricing activities.

At the same time, the industry must remain pragmatic. P&SA has conducted several broad and focused investigations relative to industry structure and marketing practices, and has taken enforcement actions when necessary to address infractions. However, repeated anti-trust investigations by P&SA and the Justice department have not uncovered broad, industry-wide illegal activities. Part of the frustration in the country is that many marketing practices and industry concentration levels that are perceived to be illegal are not.

NCBA has long supported strong oversight and enforcement of existing anti-trust and market protection laws. NCBA's 1988 Beef Industry Concentration and Integration Task Force spent a year evaluating this issue in anticipation of ongoing industry restructuring. The GAO has conducted repeated studies going back to the 1980s including "Beef Industry Packer Market Concentration and Cattle Prices," December 1990 and P&SA Oversight of Livestock Market Competitiveness Needs to Be Enhanced," October 1991.

These and other studies coupled with industry input have resulted in P&SA restructuring and modifications in enforcement and investigative activities. Change in the beef industry, as in the rest of the economy, is a reality. The global market is a reality and has necessitated changes by companies to maintain competitiveness in the international marketplace. Efforts to inhibit or roll back change in the beef industry will only result in policy-imposed inefficiencies and lack of competitiveness for the US beef industry. This is especially true if other US meat industries and beef producers in other countries are allowed to restructure and modify marketing practices in response to changing realities of the marketplace.

New Marketing Systems:
In addition to increasing concentration, there has been a trend toward alignment between packers and feeders through contracts, marketing agreements and custom feeding of packer-owned cattle. NCBA policy is specific regarding these emerging business relationships.

- NCBA will not recommend the limitation of any method of marketing fed cattle.
- NCBA supports a free market system.
- No action is to be taken to alter or halt current trends toward private business arrangements among operators in the various sectors of the beef industry.
- NCBA is to encourage producers -- individually and through cooperative efforts -- to take advantage of opportunities to increase profits through new marketing strategies, coordination, risk management and retained ownership.

A number of producers are finding innovative ways to compete in the changing beef industry including gaining a greater share of the marketing dollar. There are several examples representing different approaches by groups of cattle producers, such as:

- U.S. Premium Beef, Ltd.
- Western Beef Alliance
- Ranchers' Renaissance
- Iowa Cattlemen/Excel joint venture
- Angus Alliance
- Five-State Beef Initiative
- Harris Ranch
- Nichols Farms Alliance

These are just a few of the innovative marketing available. There are many more, particularly in areas where producers are teaming with other segments of the industry to take advantage of national, regional and even niche market opportunities.

This growing number of innovators are long-term professional cattlemen who came together to address their desire for a growing, viable beef industry in a proactive way by developing bold new marketing strategies. No longer are these producers' energies consumed by concerns about market structure. Their efforts revolve around producing a better beef product that is marketed through their own beef company. As owners, these cattlemen receive rewards from a value-based pricing system, individual carcass data and earnings from the company at year-end.

NCBA and the beef industry must ensure that legislative and regulatory policies continue to encourage these types of solutions and do not limit a producer's ability to gain a greater share of the marketing dollar. Much of the discussion and debate among thought-leaders in the industry has been about how to foster new marketing systems that meet consumer needs and increase beef demand. Participants in the deliberative process have been very concerned about the "law of unintended consequences" as we worked to develop processes that would increase information flow and market transparency without unintentionally placing new and innovative marketing systems at a competitive disadvantage.

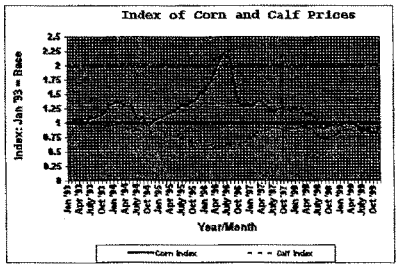
While the beef industry continues to debate concentration and marketing system issues, there is widespread agreement that efficient markets require greater market transparency that is achieved by the availability of accurate and timely information -- especially in situations with many sellers and few buyers. Information availability helps ensure that competitive market forces exist. Fewer buyers cannot have undue leverage when market information is widely available to more dispersed sellers. Consistent with legislation approved last year NCBA urges USDA to aggressively pursue implementation of mandatory price reporting for cattle, boxed beef, imports and exports.

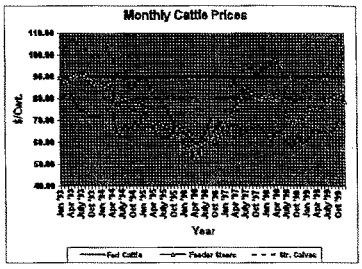
Improving Market Conditions:
The beef industry is in many ways a bright spot among many depressed agricultural commodities. In part, this is because we have never relied on the government to "fix" industry conditions caused by market forces. Because of this, we are not making a difficult transition from government programs to reliance on private sector market forces. Cattlemen have always had the "freedom to farm" and the freedom to fail. With this historical backdrop it may be easier for the Committee to understand why there is a great deal of caution and reluctance throughout the mainstream beef industry to call for dramatic expansion of government intervention in the beef industry marketplace. We remain committed to strong oversight and enforcement of existing laws and regulations.

While we empathize with current low prices experienced by grain producers in the face of recent record production -- prices for calves and yearlings have increased and farmers and ranchers are recovering from the crisis of 1996.. Prices for steer calves and feeder cattle are again higher than fed cattle prices. Increased fed cattle prices since March 1999 and cautious optimism have resulted in continued increases in prices for calves and feeder cattle.

Prices for all classes of cattle are significantly improved from the cyclical lows established during 1996, but still below the cyclical high prices of the early 1990s. During March and April 1996, the

monthly average prices for steer calves averaged less than $60/cwt. and feeder cattle prices averaged less than $54/cwt. These prices were a major decline from prices experienced during the late 1980s and early 1990s and were directly related to cyclical increases in cattle numbers and record high grain prices.





Conditions have improved dramatically since the doldrums of the mid-1990s. Prices for steer calves averaged $102.60/cwt. during December 1999 -- the first time the monthly average has exceeded $100/cwt. since April 1994. Prices for steer calves have generally ranged above $90/cwt. since January 1999. Fed cattle prices averaged nearly $70/cwt. during November 1999 and are projected to improve to the low $70s/cwt. next spring as cattle numbers continue to decline. Higher cattle prices are primarily due to declining numbers of calves and feeder cattle, improving beef demand after a 20-year decline, improvements in Asian financial conditions resulting in improved by-product values and general improvement in export markets.

As stated at the outset, of this testimony NCBA and the beef industry support Justice Department and P&SA enforcement of the P&S Act as amended and anti-trust laws and regulations. We support timely and complete USDA implementation of mandatory price reporting legislation passed last session. We urge that USDA be involved in pre-merger evaluation of proposed packer mergers in coordination with evaluation by the Justice Department and support adequate funding for GIPSA and the Justice Department to accomplish their investigative functions.

NCBA supports a free market system and we trust in the ability, adaptability and innovating skills of the US cattleman to be able to prosper in a relatively unregulated domestic and international marketplace. We rely on federal regulators to ensure that the marketplace is free from anti-trust, collusion, price fixing and other illegal activities that damage the viability of the market and interfere with market signals, but also to keep the playing field level for cattle producers. If allowed to work the market will recover with a minimum of government intervention and cost of regulatory inefficiency. To remain competitive in a global market, this is absolutely a necessity.

We are prepared to work with you and your staff to provide additional information and direction. Again, we certainly appreciate the leadership the Committee has shown in addressing the tough issue of an evolving competitive industry structure and the appropriate role of government oversight.

Thank you for the opportunity to present this information.

STATEMENT OF THE

NATIONAL CHICKEN COUNCIL

REGARDING PACKERS AND STOCKYARDS ADMINISTRATION OVERSIGHT

HEARING OF THE COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY

THE HONORABLE RICHARD G. LUGAR CHAIRMAN

PRESENTED BY
WILLIAM P. ROENIGK
SENIOR VICE PRESIDENT
NATIONAL CHICKEN COUNCIL

TUESDAY, FEBRUARY 1, 2000

1015 15TH STREET, NW, SUITE 930, WASHINGTON, DC 20005

Thank you, Chairman Lugar, Senator Harkin, and Committee Members for the opportunity to present our views on a very important issue. 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 processing and contract with breeder farmers to supply fertile eggs for hatching. The system of production, processing and marketing is highly coordinated and operates very much in a just-in-time method. During the 1950s and 1960s the system evolved into the vertically-integrated structure that has been the standard business model for five decades. 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.

With respect to one of the specific issues being addressed today, the National Chicken Council (NCC) is opposed to the U.S. Department of Agriculture having expanded regulatory authority over poultry production because such additional power is unnecessary. Adequate authority and remedies already exist.

In 1987, Congress fully and carefully considered the proper scope of USDA's Grain Inspection and Packers and Stockyards Administration's (GIPSA) administrative enforcement authority (including civil money penalty authority) with respect to transactions involving live poultry and poultry products. Congress declined to provide such 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 nor developments that have occurred since 1987 that would warrant Congress reversing its decision.

GIPSA argues that it needs authority to proceed administratively against, and impose civil penalties on, poultry processors that violate the P&S Act's prohibition against unfair or deceptive practices because it has such authority already for the red meat industry. GIPSA, together with other government agencies, however, already have more than enough authority to ensure fair dealing within the poultry industry. First, as alluded to earlier, 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.

Secretary of Agriculture Dan Glickman in his transmittal letter of June 8, 1999 to the Congress regarding the draft bill to amend the P&S Act stated "This proposed bill would permit USDA to pursue violators quicker and cheaper. . . ." The Secretary was making reference to live poultry dealers who violate the Act's Section 202 (unfair practices). It is fair to ask if "quicker and cheaper" should be the guiding principles with respect to whether or not expanded authority is needed. A more basic question would be "Is expanded authority truly necessary?"

Another very important and fundamental question is, "has GIPSA provided documented examples of where cases of unfair practices involving poultry have been unresolved because the system of referring cases to the Justice Department did not operate satisfactorily?" It would be premature to try to "fix" a mechanism we have not even determined to be broken.

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 the beef industry where cow-calf producers sell calves to dealers who deliver the calves to feedlots who fatten the cattle for eventual sale to a slaughterer. Although the hog industry's structure and business model are changing, the Act reflects the traditional system of pork production. 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 red meat industry, 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 a very important, but often overlooked in the discussion of the broader issue.

We appreciate the opportunity to share our views and position.

Statement of the American Farm Bureau Federation

TO THE
SENATE AGRICULTURE, NUTRITION AND FORESTRY COMMITTEE
REGARDING
THE CONCENTRATION OF BUSINESS OWNERSHIP IN THE AGRICULTURE SECTOR

Presented by:

Ron Warfield, President
Illinois Farm Bureau

February 1, 2000

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As the national voice of agriculture, AFBF's mission is to work cooperatively with the member state Farm Bureaus to promote the image, political influence, quality of life and profitability of the nation's farm and ranch families.

FARM BUREAU represents more than 4,800,000 member families in 50 states and Puerto Rico with organizations in approximately 2,800 counties.

FARM BUREAU is an independent, non-governmental, voluntary organization of families united for the purpose of analyzing their problems and formulating action to achieve educational improvement, economic opportunity and social advancement and, thereby, to promote the national well-being.

FARM BUREAU is local, county, state, national and international in its scope and influence and works with both major political parties to achieve the policy objectives outlined by its members.

FARM BUREAU is people in action. Its activities are based on policies decided by voting delegates at the county, state and national levels. The American Farm Bureau Federation policies are decided each year by voting delegates at an annual meeting in January.

STATEMENT OF
THE AMERICAN FARM BUREAU FEDERATION
TO THE
SENATE AGRICULTURE, NUTRITION AND FORESTRY COMMITTEE
REGARDING
THE CONCENTRATION OF BUSINESS OWNERSHIP IN THE AGRICULTURE SECTOR

Presented by:

Ron Warfield, President
Illinois Farm Bureau

February 1, 2000

Good morning, Mr. Chairman. My name is Ron Warfield. I am the president of Illinois Farm Bureau and a member of the executive committee of the American Farm Bureau Federation. I have a farming operation in Gibson City, Illinois and grow corn and soybeans. Today, I am testifying on behalf of the American Farm Bureau Federation which is the nation's largest general farm organization, representing over 4.9 million member families in all fifty states and Puerto Rico.

We appreciate the opportunity to testify on the Grain Inspection Packers and Stockyards Administration (GIPSA.) We work closely with GIPSA on a number of issues and have policy stating that we support the continuation of GIPSA as a separate agency of USDA and oppose any attempt to lessen the ability of this agency to adequately enforce the act and its regulations. We have also expanded our testimony to include the broad issue of concentration for today's hearing.

Producers across the country continue to struggle to meet their costs of production. Consider the following:

- over the past 18 months pork producers have lost over $4 billion in equity alone due to collapse of the hog market;
- the beef industry has also experienced a $4 billion loss in the past five years;
- the poultry industry is already over 90 percent vertically integrated and has unique concerns, most notably contract negotiations;
- profit margins for producers are very slim and there is great concern regarding the widening farm-to-retail price spread;
- the growing use of patents on biotech seeds puts the ownership of germplasm in the hands of relatively few companies;
- disruptions in the rail industry and lack of competitive transportation options due to recent railroad mergers; and
- for 2000, USDA projects a substantial decline in farm income and an increase in production expenses.

It is no wonder that an already large and growing number of U.S. producers have become increasingly concerned regarding the continued loss of equity and the outlook for restoring profitability in agriculture.

We understand that agribusinesses, just like farmers, will have to adjust and adapt in order to compete in today's global economy. Our primary concern is that with these changes we maintain markets that continue to function in a way that are free and open, competitive, with transparent and clear price signals that continue to give farmers options and opportunities for both purchasing inputs and selling their products.

Farm Bureau has been working aggressively to address the issue of obtaining more market leverage for producers within the challenging and competitive marketplace. We have had several meetings with GIPSA and the Department of Justice (DOJ) along with representatives from private industry to gain a better understanding of the laws and the process and current enforcement procedures. Concentration is a very complex and challenging issue, and Farm Bureau members judge it as a top legislative priority. We are continuing our work to seek a bi-partisan consensus among farmers, ranchers, legislators and the administration to address the complex issues at stake.

AFBF voting delegates last month adopted new policy language regarding the Packers and Stockyards Act and monopolies. Our policy states:

> The Packers and Stockyards Act should be amended to:
>
> 1) extend prompt pay requirements to wholesalers and retailers of livestock products;
> 2) include a dealer trust provision;
> 3) provide jurisdiction and enforcement over the marketing of eggs as already exists for poultry meat;
> 4) strengthen the ability of GIPSA to stop predatory practices in the meat packing industry; and
> 5) provide producer restitution when a case is successfully prosecuted.
>
> Under policy regarding monopolies, we state:
>
> We believe that consolidation, and the subsequent concentration within the U.S. agricultural sector is having adverse economic impacts on U.S. family farmers. To address this trend, we believe Congress should review existing statutes, develop legislation where necessary and strengthen enforcement activities.
>
> We support the following changes to antitrust statutes and regulations that will further protect the sellers of commodities from anticompetitive behavior:

1. The Department of Justice should ensure that proposed cooperative and/or vertical integration arrangements, if implemented, should continue to maintain independent producers access to markets;
2. USDA should be given authority to review and provide recommendations to the Department of Justice on agribusiness mergers and acquisitions;
3. A high level position should be established within the Department of Justice to enforce antitrust laws in agriculture; and,
4. USDA should be empowered to investigate mergers, consolidation or concentration of agricultural input suppliers and processors for antitrust or anticompetitive activities.

Regarding the Packers and Stockyards Act, GIPSA should be able to evaluate actions taken by packers who purchase plants and then shut them down. This has the effect of limiting competition in the area and reducing the number of marketing opportunities for independent producers. While GIPSA should balance the capacity needs, environmental considerations and other financial issues of the packers, these actions are contributing to concentration within the meat packing industry. An example would be Calhoun Beef Processors in Texas and Tama Packing Company in Iowa. Iowa Beef Processors (IBP) purchased both of these plants and subsequently closed both plants. The Tama Packing Company was closed three years after it was acquired by IBP.

Farm Bureau was very pleased with the passage of Mandatory Livestock Reporting legislation last session. This is not the "silver bullet" producers are looking for, but at least makes an effort at getting producers more market information on livestock transactions, including contractual agreements. The raw data that Agricultural Marketing Service (AMS) will collect may be very useful to GIPSA's oversight of the meat packing industry. As AMS implements mandatory price reporting, we hope they will coordinate with GIPSA to ensure that the appropriate information is collected to help in this oversight.

We have worked on an annual basis seeking additional appropriations for GIPSA in order to adequately enforce the Packers and Stockyards Act. GIPSA continues to move forward to provide resources in the country to investigate anti-competitive pricing practices. Farm Bureau members would like to see more information on these investigations, the results of the findings and whether civil penalties were imposed. We know that much of this information is confidential and cannot be released. However, we would like to take this opportunity to request GIPSA provide more information regarding:

1. Number and types of on-going investigations
2. Past investigations that resulted civil penalties being imposed
3. Total amounts of the penalties imposed
4. Current GIPSA activities that would be beneficial to producers

Critics of concentration reform and expansion of USDA authority have stated that prices are the driving force behind much of the farmers and ranchers' concerns about the issue at

the county level. We doubt that improved prices will eliminate producer concerns regarding concentration. Instead, our members suggest that "being kept in the dark" is the driving force behind their desire for reform. As is basic human nature, anyone provided limited information becomes highly skeptical, no matter the circumstances. Farmers become especially skeptical when no information is forthcoming and the result is a constriction of the number of marketing outlets in their local area. The transparency of information regarding mergers, acquisitions and anticompetitive activities must be enhanced.

Farm Bureau would like to see an expanded role for USDA in evaluating agribusiness mergers and acquisitions currently required to be evaluated by the Justice Department. Broadened USDA responsibility and official consultation with DOJ will ease much of the concern in the country regarding the concentration of agribusiness. Farm Bureau would like to see the following actions to help restore a competition-driven agriculture:

1. Expanding USDA's role in evaluating agribusiness mergers and acquisitions. Specifically, USDA should conduct a review and analysis on the proposed mergers or acquisition and then recommend to DOJ whether the proposal should be granted. An analysis and impact statement used to reach that recommendation should be disclosed to the public upon transmission to the DOJ. USDA's review should consider the following:

    a) the affect the acquisition or merger will have on prices paid to growers due to reduced opportunities to bargain with more buyers;
    b) the likelihood that the acquisition or merger will result in significantly increased market power for the new entity;
    c) the likelihood that the acquisition or merger will increase the potential for anticompetitive or predatory pricing action; and
    d) whether the acquisition or merger will adversely effect producers on a regional basis.

2. Farm Bureau supports appointing an Assistant Attorney General at DOJ with the sole responsibility of handling agriculture mergers and acquisitions. DOJ has an enormous job these days with consolidations and mergers in so many industries, much less agriculture. Counsel specifically focused on agriculture would be able to give the time necessary to make certain that the proposed consolidation would be best for all stakeholders. This position should be created at a high enough level that would require Senate confirmation.

3. Provide additional resources in order to expand the capability of GIPSA to monitor, investigate and pursue the competitive implications of structural changes in the meat packing industry. A portion of these additional resources should be specifically earmarked for increasing the number of litigating attorneys available to GIPSA to allow it to more comprehensively and effectively pursue its enforcement activities.

4. Support an increase in the staff of the Transportation, Energy and Agriculture section of the DOJ. Increase the current filing fee for each acquiring firm under premerger notification provisions of the Hart, Scott, Rodino (HSR) amendment of 1976. Currently under HSR, a transaction must be noticed to DOJ and the Federal Trade Commission if one firm has assets or annual sales of $10 million or more, the other has assets or annual sales of $100 million or more and the transaction is valued at $15 million or more (or involves 50 percent or more of the voting securities of an entity valued at $25 million or more). The acquiring party must pay a filing fee of $45,000. Additional fees should be earmarked to pay the cost of staff increases.

5. Prohibit the enforcement of confidentiality clauses in livestock production contracts and grain production contracts except to the extent a legitimate trade secret is being protected. The objective of such legislation would be to bar the enforcement of those confidentiality clauses which are overly broad in that they seek to prevent dissemination of information about the material terms and conditions of contracts without any legitimate trade secret basis. The primary practical effect of such provisions appears to be to inhibit producers from discussing, comparing and contrasting the differing types of contractual arrangements with their bankers, lawyers and accountants.

6. Allow GIPSA to ask for reparations for producers as well as civil penalties when a packer is found to be engaged in predatory or unfair practices.

7. Require USDA to gather, maintain and disseminate upon request, detailed information relative to corporate structure, strategic alliances, joint venture and the like for all agribusiness entities with annual sale in excess of $100 million annually.

8. Provide contract poultry growers the same protections as livestock producers by extending the powers of GIPSA to cover live poultry dealers in the same fashion as packers of cattle and swine are covered and, in addition, extend the authority of GIPSA over poultry and domestic fowl raised for non-slaughter purposes.

9. Allow the USDA's Rural Business and Industry Guaranteed Loan Program to make loan guarantees to farmer-owned projects that add value and are sited in urban areas exceeding a population of 50,000 people. A group of turkey producers are interested in developing a value-added processing facility in Michigan and are seeking the assistance of the Rural Business and Industry Guaranteed Loan Program. The plant that they wish to acquire is located in a city with a population over the cap of 50,000 people.

10. Authorize a statutory trust for the protection of cash sellers to livestock dealers.

We are working with several senators to develop legislation and seek bipartisan support to address these issues and attain a competitive market agriculture.

In closing, we understand that agriculture is not the only sector experiencing the impacts of mergers and acquisitions. The continued weakness of the U.S. farm economy warrants timely Congressional review. Our goal is to make anti-trust statutes more relevant for today's agriculture and to see more information flow to the public with regard to investigating anticompetitive behavior within the agricultural industry. This could be achieved with expanded USDA authority and increased oversight for agribusiness mergers and acquisitions.

Again, thank you for this opportunity to share our thoughts on concentration with you. I would be happy to respond to questions.

WRITTEN TESTIMONY OF
THE ORGANIZATION FOR COMPETITIVE MARKETS
presented to the
UNITED STATES SENATE
COMMITTEE ON AGRICULTURE, NUTRITION AND FORESTRY

February 1, 2000

Structure and Authority of the
Grain Inspection, Packers & Stockyards Administration

Thank you Mr. Chairman and distinguished members of the Committee on Agriculture, Nutrition and Forestry for the opportunity to present this written testimony today for the record. My name is Michael Stumo, general counsel of the Organization for Competitive Markets. The Organization for Competitive Markets is a multi-disciplinary group dedicated to reclaiming competitive markets in agriculture for independent farmers, ranchers and rural communities. I am also a hog farmer in Massachusetts and am formerly an Iowa hog and cattle buyer.

I. Abstract

This testimony concludes that the Packers & Stockyards Act gave the Secretary extremely broad authority to preserve open and competitive markets for all farmers and ranchers. The Act was also designed to stop practices in their incipiency, before they cause harm, not after they cause harm. This testimony also asserts that the USDA Office of General Counsel has been the core source of the problem in restrictively and/or inconclusively defining the standard required to trigger the Secretary's authority. The OGC approach, or lack thereof, results in USDA-ERS and GIPSA involvement and activity which is unhelpful at best and destructive at worst.

II. Introduction

The Homestead Act of 1862 created the family farm system of agriculture. Today we are losing that system to an industry-controlled conglomeration of contracts and ownership arrangements. This new top-down system closes down the open market and allows corporate offices to go beyond merely affecting the market unduly to consciously picking and choosing who wins and who loses.

Feedstuffs magazine is the premier agribusiness weekly in this country. It primarily covers the packing, grain merchandizing, poultry, animal feed and animal drug sectors. The September 13, 1999 editorial stated, "American agriculture must now quickly consolidate all farmers and livestock producers into about 50 production systems." This closure of markets scenario is the antithesis of family farming and ranching and the antithesis of market competition. Open markets are replaced by internal complexity management in conglomerates who consciously choose who succeeds and who fails. The Packers & Stockyards Act was designed to prevent this transformation of family farmers into mere hog-house janitors.

The open market in hogs has become nearly a residual market. It may disappear in five years with all hogs under packer ownership or control. Packers pick and choose the winners and losers. In October, 1998, the top procurement people from Hormel and Excel told a group that the reasons they contracted was to guarantee supply for their plants. They consciously chose the best producers and offered contracts to them. Left unsaid is that they did not offer relationships to producers they supposedly believed were not viable. They choose the winners and losers.

Vertical integration is rapidly winnowing down the number of producers because, no matter how few producers, there will be some that packers want to contract with and others they will exclude. The Excel buyer admitted to having no contracts with small producers.

Once producers are under contract and the open market becomes a low-priced, residual market, the packer has even more power. First, the producer has no other options, witness the poultry industry contractors. The open market is essentially gone and other integrators are few. Second, the contract gives the packer more mechanisms to force risk and cost onto the producer in the so-called integrated production system. The producer has become a cost center, something the packer wants to and can reduce. One producer recently told an OCM member that Farmland was forcing a new contract upon him which would reduce his revenue by $109,000 per year. While he has not agreed to the new contract yet, his alternatives are few.

Rather than paying for quality in the open market, packers are forcing management decisions, risk and cost upon producers with the onerous terms of contracts.

The Packers & Stockyards Act (the Act) is one of the strongest competition laws ever written in this country. It is designed to preserve market competition and stop problematic practices at their incipiency, before they cause harm.

USDA has failed to use its authority under the Act, whether through regulation or enforcement. It is a truism that if you do not exercise authority, that authority will wither away and eventually cease to exist. USDA's failure to exercise its regulatory or enforcement authority has rendered it impotent in the face of the rapid consolidation of the industry which is presenting the "end game" for family farm agriculture. The source of these problems is in three USDA agencies: (1) Office of General Counsel; (2) Economic Research Service; and (3) Grain Inspection, Packers & Stockyards Division.

III. Purpose of the Act

Whereas general antitrust law has generally focused on harm to the consumer in recent years, the Packers and Stockyards Act clearly exists to prevent harm to producers. Harm to producers often means the risk of lower prices in the marketplace. But the means to protect producers was ensuring the most open and competitive markets possible. **The structure of the market was considered of paramount importance.**

This point is important because legislative direction to promote a competitive market structure is different than a mere mandate to prevent low prices for producers. Regulatory and enforcement authority then must focus on the conduct of market participants in making an open

and competitive market. The need to make the complex case that prices have been lowered or producers have been hurt is not the burden required.

The intent of Congress in 1921 in passing the Act was to protect the producers of meat, reduce the power of the packers, and preserve a market structure which is open and competitive rather than the closed and controlled market we have today. The legislative history is instructive.

During the contemporary debate leading up to passage of the Act, Representative Tincher stated:

> "It is my judgment that the passage of this bill, that its proper administration, will permit the meat producer to exist; that it will reduce the amount paid out between the producer and consumer to such an extent that it will make the business for the producer more profitable, and not be injurious to the consumer."

61 Con. Rec. 1809 (1921). Representative Voight of Wisconsin said:

> "I think if this monopoly of the Big Five is done away with, and the laws of trade are given a chance to function, it is going to benefit producer and consumer alike; genuine competition will benefit both."

61 Cong. Rec. 1868 (1921). Representative Jones from Texas commented on the importance of preserving an open, competitive market structure for the producer:

> "The producer must always sell in a market that he does not control. He buys at the other man's price. His only hope of securing a fair price lies in an open, competitive market."

61 Cong. Rec. 1861 (1921).

In fact, Congress viewed "unfair competition" as much broader under the Act than under the FTC Act, in contrast to the improperly limited view accorded to it by some today. Representative Anderson made this point:

> "As to the intent of 'unfair competition' [in the FTC Act] it only includes acts which constitute a violation of the rights of the competitor, and it must be a method which is used by a competitor on the same plane. *** For instance the method of competition used be a manufacturer which we might think was a violation of the moral rights of the wholesaler would not be a violation of the Federal Trade Commission Act, because the interpretation of that is that it must be unfair as between competitors who stand on the same plane. This goes further than that, as it affects the public interest to a large extent, and the unfair competition or unfair practice as between a packer and the general public, the packer and the producer, or the packer and any other agency connected with the marketing of livestock."

61 Cong. Rec. 1805 (1921).

The legislators of the time viewed an open and competitive market structure to be in the public interest. This contrasts with the closed and controlled structure advocated by industry today. It also contrasts with recent views of the USDA that the Secretary must prove a strong likelihood of competitive injury - meaning lower prices - and/or predatory intent. These views exist despite the fact that subsections (a) and (b) of section 202 of the Act have no requirement of proving intent to harm competition or to prove that prices are manipulated, while subsections (d), (e) and (f) do include such requirements.[1]

This USDA position has resulted in court decisions which effectively codify the competitive injury and predatory intent burdens. See, IBP, Inc. v. Glickman, No. 98-3104 (8th Cir. 1999).

The Congress should reaffirm the original intent of the Act in that it is designed to produce an open and competitive market structure without regard to intent or proof of injury. This would give the Secretary and the courts proper guidance in protecting producers of meat.

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[1] **Sec. 192. Unlawful practices enumerated**

It shall be unlawful for any packer with respect to livestock, meats, meat food products, or livestock products in unmanufactured form, or for any live poultry dealer with respect to live poultry, to:

(a) Engage in or use any unfair, unjustly discriminatory, or deceptive practice or device; or

(b) Make or give any undue or unreasonable preference or advantage to any particular person or locality in any respect whatsoever, or subject any particular person or locality to any undue or unreasonable prejudice or disadvantage in any respect whatsoever; or

(c) Sell or otherwise transfer to or for any other packer or any live poultry dealer, or buy or otherwise receive from or for any other packer or any live poultry dealer, any article for the purpose or with the effect of apportioning the supply between any such persons, if such apportionment has the tendency or effect of restraining commerce or of creating a monopoly; or

(d) Sell or otherwise transfer to or for any other person, or buy or otherwise receive from or for any other person, any article for the purpose or with the effect of manipulating or controlling prices, or of creating a monopoly in the acquisition of, buying, selling, or dealing in, any article, or of restraining commerce; or

(e) Engage in any course of business or do any act for the purpose or with the effect of manipulating or controlling prices, or of creating a monopoly in the acquisition of, buying, selling, or dealing in, any article, or of restraining commerce; or

(f) Conspire, combine, agree, or arrange with any other person
(1) to apportion territory for carrying on business, or (2) to apportion purchases or sales of any article, or (3) to manipulate or control prices; or

(g) Conspire, combine, agree, or arrange with any other person to do, or aid or abet the doing of, any act made unlawful by subdivisions (a), (b), (c), (d), or (e) of this section.

IV. Office of General Counsel

The Office of General Counsel is the primary source of the problem of nonexistent P&S enforcement. It has obstructed USDA-GIPSA from using its regulatory and enforcement authority under the Act by taking incorrect positions as to the scope of that authority and by failing to concretely define the factors as to what it believes constitutes violations of the Act. Thus, the meaning of the Act has become uncertain at best for producers and packers and irrelevant at worst. GIPSA does not know what type of case to build in order to enforce the Act. Further, OGC lacks the expertise to litigate complex anticompetitive practices case. The result is lack of a defined framework within which true competition can flourish.

A. Preserving open and competitive markets vs. proof of injury

If the original intent of the Act where pursued, the Secretary could utilize section 202(a) and (b) (7 U.S.C. 192(a) and (b)) to preserve open and competitive markets for producers without regard to proving harm or a likelihood of harm. As the Congress of 1921 recognized, preserving open and competitive markets is a policy goal in and of itself. The Congress made the connection between such a market structure and a likelihood of producer injury. It is redundant for either the Secretary or the courts to require such a connection before enforcement occurs.

But with the current judicial gloss on the Act, caused in part by USDA's improper view of its own authority, Congressional action is needed to return to its original purpose. Consider how the Act has been distorted.

In 1968, the Court in Armour & Company v. United States stated:

> "The clearer the danger of the [likelihood of competitive injury], as when competitors conspire to eliminate the uncertainties of price competition, the less important is proof of [predatory intent]. Conversely, the likelihood of injury arising from conduct adopted with predatory purpose is so great as to require little or no showing that such injury has taken place."[2]

The position of OGC is that:

> "In order to prohibit activities of the packers through regulation or [enforcement], the Department must develop evidence that the packers have either predatory intent or that there is the likelihood that the complained of activity will result in injury. (OGC Memorandum to the Chief Economist, June 20, 1996, p. 5 (Attachment 2)."[3]

The OGC position results in lack of historic regulatory activity which defines unfair and unjustly discriminatory practices or undue or unreasonable preferences. Thus, without such

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[2] 402 F.2d 712, 717 (7th Cir. 1968).

[3] "Review of Western Organization of Resource Councils (WORC) Petition for Rulemaking," Grain Inspection and Packers and Stockyards Administration, Packers and Stockyards Programs, August 29, 1997.

definition, the Courts have filled the void and placed more restrictions on the Secretary's authority. These restriction include importation of a "predatory intent" requirement from general antitrust law, and a more stringent and narrow reading of the "likelihood of harm" approach.

B. Rulemaking

Administrative rulemaking would have been the proper way to keep up with the industry and stop unfair trade practices "in their incipiency, before harm has been suffered." Farrow v. USDA, 760 F.2d 211, 215 (8th Cir. 1985). Preventing the closure of the open market decades ago would have enabled today's independent producers access to markets regardless of their size or connections.

The key here is the "likelihood of harm" standard. While OCM believes that the Act is focused on open and competitive markets and that Congress has already made the connection between that goal and harm to the producer, the present view of that standard is now important.

The spectrum of views on "likelihood of harm" ranges from the "incipiency" view on one end and the "proof of past harm" on the other end. The OCM and others subscribe to the forward looking "incipiency" view, i.e. that a practice must be stopped at the outset if proliferation would be likely to cause harm to open and competitive markets in the future. The OGC and some courts have taken a position nearing backward looking "proof of past harm" view. This restrictive view requires tremendous economic analysis of past data to show that an established practice is making prices trend lower. Thus, the central role of USDA-ERS in these issues.

While the USDA-OGC view is quite restrictive, but amorphous. While OGC often states what is not a violation of the Act, it never states what is a violation of the act.

But the lack of a departmental position - whether through rulemaking or through internal guidelines - has resulted in USDA struggling to define violations of the Act on a case-by-case basis through enforcement. This ad hoc approach has, in turn, resulted in conflicting caselaw. For example, in the Eighth Circuit alone, the legal standard for USDA authority under the Act can be read to range from no requirement to prove injury (Farrow v. USDA, 760 F.2d 211, 215 (8th Cir. 1985), (stating that the act does not require the USDA to prove actual injury before a practice may be found unfair)) to statements appearing to require actual proof of injury (IBP, Inc. v. Glickman, No. 98-3104, pp. 4-5 (8th Cir. 1999) (finding no evidence to show actual harm to producers in that case)).

The Western Organization of Resource Councils recently submitted a Petition for Rulemaking to the USDA. OGC took the position that the economic evidence did not meet the standard for showing likelihood of injury.[4] Not only did the OGC's position border on requiring proof of injury, but, in meetings with WORC staff, OGC failed and refused to give information as to what does meet their opinion as to the standard. GIPSA has the same problem with OGC - "Don't just say what does not meet the standard, tell us what does meet the standard."

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[4] Id.

Because OGC appears entirely reluctant to support expansive rulemaking to preserve an open and competitive market for all producers, Congress should strongly consider enacting legislation specifically defining violations. Congress should also consider experts in administrative law and trade regulation in non-agricultural contexts to determine the regulatory power of USDA under the Act.

C. Enforcement

While the Department of Justice has the primary litigation expertise in representing federal agencies in court, OGC does little in the way of complex business litigation. However, enforcement of the Act is an exception. Under the Act, OGC prepares and litigates very resource intensive and complex cases. Unfortunately, OGC is not very good at litigating these specialized, resource intensive and complex claims involving anticompetitive practices.

It is fact that most OGC work does not involve anticompetitive practice issues. It is fact that OGC does not hire people with the requisite training and experience in such matters. In fact, the P&S Acting Deputy Administrator told the USDA's Office of Inspector General that he believed that OGC had limited expertise in these issues.[5] P&S officials told OIG "that OGC does not want to litigate anticompetitive cases because they are complicated and time consuming."[6]

The fact that OGC lacks the expertise and the desire to enforce the Act combined with the fact that OGC has a poor track record when it chooses to do so, strongly suggests that enforcement should be transferred to the Department of Justice. This is more fully explored below.

V. Economic Research Service

Under the present regulatory approach, i.e. past harm must be shown to trigger regulation or enforcement, ERS must show that packer concentration or captive supply reduces prices to producers before regulations or enforcement commence. If OGC took the position that preserving an open and competitive market was the policy goal, or at least adopted the incipiency test, the onus on ERS would not be so large. But, given this onus, ERS has failed.

In order to find a connection between industry structure and lower prices, the right data must be available, the right questions must be asked, the right models must be used, and the right people must interpret the models. ERS does not ask the right questions. ERS cannot or does not procure the right detailed data. ERS does not perform the proper econometric studies to isolate cause and effect between various factors, including concentration and captive supply, and price. ERS has failed to define geographic market areas from which to determine market concentration and harm to regional producers. ERS has failed to perform forensic economic investigations, with subpoenaed data, into packer practices.

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[5] "Grain Inspection, Packers and Stockyards Administration, Evaluation of Agency Efforrts to Monitor and Investigate Anticompetitive Practices in the Meat Packing Industry," USDA-OIG, Evaluation Report No. 30801-0001-Ch, pg. 19, February, 1997.

[6] Id.

Rather ERS, and its contracted outside researchers, have relied upon voluntarily disclosed packer data, plus aggregate publicly available data, to repeatedly conclude that they find no evidence of packer concentration affecting prices. A controversial ERS report released May 4, 1999 and entitled "US Beef Industry: Cattle Cycles, Price Spreads and Packer Concentration," concluded that there was no evidence that packer concentration did not affect prices. Yet it had no data or methodology designed to answer such a question. In fact, the original purpose of the study included no mention of monopoly pricing. Nonetheless, somebody decided, at the last minute, to throw in false conclusions about the effect, or lack thereof, of packer concentration on market prices. A more reasonable conclusions would be to state that "there is no evidence to show that packer concentration did not affect prices." ERS credibility is waning on industry structure and pricing issues.

Congress should ask the Department of Justice what type of data and methodology is needed to determine anticompetitive practices or market power. It is likely they will find the ERS approach lacking. For ERS to do a competent study, they at least need date pricing (price of cattle on date of agreement, not date of delivery) and time pricing (time of day cattle are priced). Without date pricing, there are gaping holes in short term price trends which have major impacts on packer profitability. Time pricing is needed to determine whether packers such IBP are price leaders - as many in the industry believe - with other packers following when the market is set by that price leader. Additionally, though overt captive supply[7] livestock percentages are very high, many marketing agreements (a form of captive supply) are oral - not written - and thus not taken into consideration.

With the ERS position that concentration and captive supply does not hurt prices, GIPSA and OGC must hew to that position in administering the Act. It is difficult for USDA to allege, in an enforcement action, that certain practices are anticompetitive when ERS says the industry is competitive. Especially given the OGC belief of some amorphous, but high, standard requiring nearly proof of actual past harm to trigger the Secretary's authority under the Act.

VI. GIPSA

Since the 1997 OIG report recommending reorganization of GIPSA into fewer and bigger specialized offices, GIPSA has done so. However, when GIPSA investigative staff respond to producer complaints, they tell producers that it is unlikely they can do anything because they lack the resources to act quickly and effectively. GIPSA is rumored to have difficulty hiring econometricians because quality people achieve higher wages in the private sector. Further, OGC still has not given GIPSA specific guidance on what factors to look for in order to prove a violation of the Act.

Further, GIPSA has put no internal guidelines in place for collecting the right information for an anticompetitive practices case. It has no guidelines or standards which would create "red flags" if certain information came to them indicating a violation of the Act. Thus, they are adrift, perhaps irrevocably so.

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[7] "Captive supply" includes packer owned livestock as well as livestock deliveries controlled by packers through forward contracts and marketing agreements.

VII. Transferring enforcement jurisdiction to the Department of Justice

The aforementioned barriers to effective enforcement of the Act by USDA are institutional and persistent. Congress is unlikely to correct them merely through legislation or brow-beating, although these approaches are helpful. The Department of Justice has the expertise to perform the investigation, economic analysis and legal analysis necessary to enforce trade regulations. A separate office within Justice is likely the best possibility for quality enforcement in the public interest.

The potential problems with such a change in jurisdiction is that agriculture could be forgotten in the shadow of "sexier" issues such as competition in technology, health care, airlines, etc. Also, importation of a general antitrust law mentality into enforcement of the Act could dilute its significance. (Court decisions reading antitrust principles into the Act have served to weaken, rather than strengthen it).

But if Justice could provide the multidisciplinary expertise and enforcement, while giving agriculture the special attention it deserves, competitive markets are more likely to be preserved for independent agriculture. The experience of nearly 80 years of jurisdiction under USDA has been a tragedy.

VIII. Transferring regulatory jurisdiction to the Federal Trade Commission?

Justice does not propound regulations, it enforces and litigates. The USDA has proven a better promoter of agricultural industrialization than a regulator of it. FTC has decades of experience in propounding regulations under trade statutes. Perhaps further thought should be given to placing the regulatory authority under the Act with the FTC.

IX. What can Congress do?

Congress could modify the Act in the following ways:

1. Amend the Act to clarify that:
   a. packer ownership and control (direct or indirect) is inherently preferential and a per se violation of the Act;
   b. price discrimination is unfair except as to quantifiable differences in quality and transportation costs;
   c. forward contracts and marketing agreements are per se preferential unless traded on an open, publicly reported market;
   d. no proof of intent is required to show a violation of 7 U.S.C. 192(a) or (b);
   e. the policy goal is to maintain the most open and competitive market possible for all producers of all sizes and locales;
   f. the intent is to halt unfair practices in their <u>incipiency</u>, before harm has been suffered;
   g. antitrust laws do not impact the interpretation of the Act.

2. Transfer anticompetitive practices enforcement jurisdiction under the Act from USDA-GIPSA to the Department of Justice.
3. Consider the transfer of regulatory jurisdiction under the Act to another agency such as the FTC.
4. Direct the Secretary to propound regulations:
   a. defining violations of 7 U.S.C. 192(a) and (b) under the newly clarified standards and with a finite deadline. Enforce the deadline with a significant cut in program funds if the deadline is not met;
   b. requiring public trading of forward contracts so they are open for bidding and not preferentially offered.

Thank you for your time and attention. I am happy to answer any questions. My contact information follows.

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John Crabtree
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Testimony before the Senate Committee on Agriculture, Nutrition, and Forestry

Mr. Chairman, Senators, thank you for inviting me here today. My name is John Crabtree and I lead the Market Structure Project at the Center for Rural Affairs in Walthill, Nebraska.

In December 1998 and January 1999 prices paid to farmers for their market hogs dropped to unprecedented lows, as I'm sure that we all remember all too well. Over the last year prices have risen to barely profitable levels, and family farmers have left or been forced out of hog production in droves.

Meanwhile, meatpackers have continued to expand their production, either by building more industrial-scale facilities or by acquiring other pork production companies. Nowhere has this consolidation binge been more breathtaking than in Smithfield Foods' effort to add approximately 630,000 sows to their production. Although this consolidation effort is now taking a slower road, due both to decisions internal to Smithfield Foods and to recent legal challenges by the Attorneys General of Iowa and Missouri, increasing packer ownership of livestock remains one of the most salient issues facing rural America today.

Livestock production in the Midwest and Great Plains has always been a family farm and ranch enterprise. Today, we are replacing those sustainable, efficient (yes, efficient) family farms with a virtual handful of industrial, vertically integrated operations. We are only at the beginning of the economic debacle that we face if we allow family farm livestock production to become a thing of the past. In a recent *Des Moines Register* editorial, Chris Petersen, a pork producer from Clear Lake, Iowa and a close personal friend, lamented that "You'll miss us when we're gone." He was right in more ways than most of us care to imagine.

A vision of the future of rural America dotted only with packer-owned, industrial hog operations is untenable. The doomsday predictions for family farm livestock producers also discounts the hopes and dreams of the very farmers who have built their lives around livestock production and created a livestock production system in this country that is the cornerstone of our agricultural economy. Why should we accept the destruction of family farm livestock production? Many tell us that it is inevitable. The truth is another matter. We have been told time and again that large-scale, vertically integrated livestock production facilities can do a better, more efficient job of raising livestock. Research tells us a different story. Iowa State University economist Mike Duffy's research analysis of farm records of actual Iowa farms demonstrates that economies of size run out at about 150 sows farrow-to-finish. The most efficient one-third of hog producers in the University of Nebraska Swine Enterprise Records

Program sold 2,678 pigs in 1996, an average of 700 *fewer* pigs than the least efficient one-third. There is another path. Farmers and ranchers over the last year have fought furiously to create the kind of future in livestock production that they want. They have asked for nothing more than access to a marketplace and the chance to compete on a level playing field, something that has consistently been denied them of late.

For years, the Center for Rural Affairs, other farm organizations, and the farmers and ranchers that support our work were told that mandatory livestock price reporting was outside of the political reality. Then, in 1999, something amazing happened. Farmers and ranchers from throughout rural America started coming together to change that political "reality." They found some state legislators who agreed with them about the need for competition in livestock markets and worked together to pass mandatory price reporting legislation in 5 states.

They didn't stop there. They changed long and closely held positions of key commodity groups, they lobbied Congress, and they kept the pressure on until mandatory livestock price reporting had changed from the impossible to a political imperative. This Committee responded by working diligently to create good, sound, strong livestock price reporting legislation which has become the law of the land. This action was not handed down from on high, it was demanded from the countryside. No single policy-maker, commodity group, or farm organization can claim credit for this effort because that honor is reserved for the farmers and ranchers that made it a reality.

The same farmers and ranchers that challenged the status quo, and won, know that the job is not done. If we are to create a future for family farm and ranch livestock production, there are more issues that must be addressed. Two needed reforms stand out.

1. Prohibiting price discrimination: When family farmers sell hogs, they get less than large-scale pork production companies for the same quality of animal just because they lack the economic power to demand volume premiums. USDA's 1996 Western Corn Belt Procurement Investigation demonstrated that prices paid to producers clearly increased with seller size. That was in 1996 when the spot market demand for hogs was probably triple what it is today. Volume-based premiums are undoubtedly more prevalent than four years ago. A clearer picture of the what actually happens in livestock markets and the extent to which family farmers are discriminated against in the market each day will become available when the mandatory livestock price reporting program is implemented. An effective price reporting program will provide important information for the Packers and Stockyards Administration to stop the routine price discrimination that occurs in livestock markets today. However, information alone will not suffice.

The Packers and Stockyards Act prohibits undue price preferences and grants USDA broad authority to stop unfair trade practices in their incipiency. That authority is unused. Secretary of Agriculture Dan Glickman recently said that USDA would "not allow farmers to become serfs on their own land" in reference to concerns about concentration and consolidation in the seed industry. This statement rings hollow when one considers that the Secretary has done

little to stop the same thing from happening to pork producers. Secretary Glickman should rectify this inaction by issuing an administrative rule that clearly defines and aggressively prohibits undue price preferences in livestock markets. The reasons for USDA's inaction on this issue are unknown to me and that inaction is, to say the least, confounding.

I have attached to my testimony language that the Center for Rural Affairs has proposed as a starting point for such a rule. This proposal recognizes that packers should be able to pay premiums for measurable and definable differences in carcass quality and transactional costs but that volume-based premiums that simply reward economic power over hard work and efficiency reduce competition and diminish the marketplace. Ever farmer and rancher that I know would be more than happy to put their hard work and skilled management up against the largest corporate hog producer in the country if they knew that they had a marketplace that would judge their livestock on a level playing field and price them accordingly.

Issuing rules on undue price preferences is not only something that USDA can do but must do if they are serious about restoring competition in livestock markets. USDA officials have argued that by defining an undue price preference the authority under the Packers and Stockyards Act will be diminished. However, since that authority is virtually unused currently, what we have today is a livestock market that has virtually no rules whatsoever regarding price discrimination.

The Center for Rural Affairs sought the legal opinion of Professor Neil Harl of Iowa State University, in this regard. I have attached to my testimony his letter in response. In this letter Professor Harl clearly points out that USDA has not fully exercised the authority granted under the Packers and Stockyards Act to promulgate rules, especially in the area of discrimination in livestock pricing. Professor Harl has also pointed out in the past that the courts will give an administrative agency leeway in enforcing market regulations if they promulgate rules that fit within the authority of that law; and that the absence of rules that allow all participants in the market, buyers and sellers, to understand the playing field diminishes the enforcement ability of an agency like the Packers and Stockyards Administration. USDA seems to have adopted the stance that volume premiums that reward economic power over hard work and efficiency are the " American way." In truth, the "American way" has always been the belief that hard work and efficiency should be rewarded and that competition enhances the marketplace.

2. Prohibit packer ownership of livestock: Last fall Senators Charles Grassley, Robert Kerrey, Tim Johson, and Craig Thomas introduced legislation to ban packer ownership of livestock. I would like to take this opportunity to thank these Senators and others who have voiced support for this legislation. Clearly, the transparency that will be acheived in livestock markets through mandatory price reporting and a prohibition of price discrimination will not alone create a future for family farmers in livestock production if the doors to the marketplace are barred to them because meatpackers own all of the livestock that they kill, from birth to slaughter, as is rapidly becoming the case in the pork sector. Legislation that prohibits or limits packer ownership of livestock is needed to kept the door to the marketplace open for family farmers and ranchers.

Thank you for your time and consideration, I would be happy to answer any questions.

Statement of

Hubert O. Farrish

Representing the

North American Export Grain Association

before the

Committee on

Agriculture, Nutrition and Forestry

United States Senate

on issues relating to the

Reauthorization of the Federal Grain Inspection Service

February 1, 2000

Mr. Chairman and Members of the Committee:

The export grain marketing and handling industry appreciates the opportunity to present its views on the role, function and performance of the Federal Grain Inspection Service section of the Grain Inspection, Packers and Stockyards Administration. This is timely as it occurs in advance of legislation being introduced to re-authorize FGIS.

I am Hubert (Bert) O. Farrish, President of Columbia Grain, Inc. which is headquartered in Portland, Oregon. Columbia is engaged primarily in the export of grain to Asia, the Middle East and Latin America. We are one of the largest users in the United States of the services provided by FGIS.

Today I am testifying on behalf of the North American Export Grain Association, an industry association representing U.S. grain exporters and associate members. I am a NAEGA Board member and chair its Grades and Inspections Committee

On September 30, 2000, five sections of the Act that created FGIS will expire. These five sections give FGIS the authority to:

1. Collect and invest official agency supervision fees for inspection (7 USC 79 (j)(4))
2. Collect original weighing service fees; collect official agency weighing supervision fees (7 USC 79A (l)(3))
3. Provide for a 40% cap for total administrative and supervisory costs (7 USC 79(d))
4. Receive Appropriations (7 USC 87h)
5. Advisory Committee Authority (7 USC 87 (j))

With the exception of the last item, without the aforementioned authority the FGIS cannot operate.

In my testimony today, I will discuss what I think the GIPSA/FGIS is doing well, how this agency could improve and the challenges for the future.

BACKGROUND:

The nature of the nation's official grain inspection system has changed and evolved since the U.S. Grain Standards Act was first adopted by Congress in 1916. The FGIS was created in 1976 and assumed the responsibilities of the Grain Division of the USDA's Agricultural Marketing Service.

The mission and activities of GIPSA, as stated in its most recent report to Congress, are:

GIPSA administers uniform, national grain inspection and weighing programs established by the U.S. Grain Standards Act, as amended. Services under the Act are performed on a fee basis for both export and domestic grain shipments. The Act requires generally that grain be inspected and weighed; prohibits deceptive practices and criminal acts with respect to the inspection and weighing of grain; and provides penalties for violations.

In administering and enforcing the Act, GIPSA:

- establishes and maintains official U.S. grain standards for barley, canola, corn, flaxseed, oats, rye, sorghum, soybeans, sunflower seed, triticale, wheat and mixed grain;
- promotes the uniform application of official U.S. grain standards by official inspection personnel;
- establishes methods and procedures, and approves equipment for the official inspection and weighing of grain;
- provides official inspection and weighing services at certain U.S. export locations, and official inspection of U.S. grain at certain export locations in eastern Canada along the St. Lawrence Seaway;
- delegates qualified State agencies to inspect and weigh grain at certain U.S. export port locations;
- licenses qualified State and private agency personnel to perform inspection and weighing activities;
- provides Federal oversight of the official inspection and weighing of grain by delegated States and designated agencies;

- provides review inspection services of U.S. grain in the United States and at certain export port locations in eastern Canada;
- investigates, in cooperation with the USDA Office of Inspector General, alleged violations of the Act and initiates appropriate corrective action;
- monitors the quality and weight of U.S. grain as received at destination ports, and investigates complaints or discrepancies reported by importers; and
- assists U.S. trading partners in developing and improving their grain inspection and weighing programs.

The Grain Standards Act provides that official inspection is mandatory at export and voluntary at domestic points. At export locations, FGIS either functions as a direct service provider or delegates it authority to state operated agencies in, for example, California and Washington State. At domestic locations, official services are provided by designated agencies which are either State agencies or privately owned companies. FGIS supervises the services provided by these agencies. Since the last re-authorization in 1993, there has been a very significant growth in the use of non-official inspection agencies for domestic grain inspections.

REMARKS REGARDING FGIS OPERATIONS:

In the view of exporters, the FGIS has two broad missions:

1. To directly provide the service of inspection and weighing grain for export or supervise delegated State agencies that provide this service.

2. To provide the structure and administration of the U.S. Grain Standards Act which benefits all segments of the grain industry including producers, processors and consumers.

My remarks will be made in the context of these two broad missions.

What are the successes of FGIS?

1. The FGIS grade and weight certificate commands respect and has great credibility and integrity with importers worldwide. From an exporter's point of view, we would not want to see any actions taken to damage this credibility. FGIS does an excellent job fulfilling the role of an unbiased entity to certify grades and weights to the export markets.

2. FGIS has responded to industry cost concerns by reducing total staff. From 1993 to 1999 total staff declined from 646 to 555 full time and 74 part time employees. Much of this personnel reduction can be attributed to reduced domestic inspections due to increased competition from private unofficial agencies. At export locations there is a greater reliance on temporary help rather than permanent employees. FGIS has reduced the cost per ton of providing the service to the industry.

3. FGIS is working with industry on a broad range of issues, including:
   A. Automated inspection procedures
   B. Biotechnology testing issues
   C. End use value characteristics in grains
   D. TCK testing for future exports to China
   E. Improved data handling and computerization of operations
   F. Computer imaging of grains for inspection purposes
   G. Standardization activities

4. FGIS has communicated well with the grain trade through its Advisory Committee and various industry committees such as the NAEGA organization has.

5. FGIS has done an excellent job in its customer outreach program.

What are areas of concern or need for improvement?

1. The battle for cost control or improvement will never end. As we are all well aware, agriculture and grain exports are an embattled industry. It is an industry constantly in search of ways to reduce costs to improve our competitive position and returns to our shareholders or owners. As long as the industry perceives itself paying more for the direct service than it believes necessary, there will be pressure to reduce costs. We need cost control but not a loss of certificate integrity. Grain inspection is still a labor intensive activity and will be for some time.

2. The twin sister of cost control is flexibility in operations. As a government agency, FGIS operates by a different set of rules than the private sector. FGIS does not have control over its personnel costs; Congress does. Personnel costs are far higher than would be the case in a similar private sector provider.

FGIS recently published notice in the Federal Register for a 2.4% fee increase due to a 4.8% mandated pay increase. Although we may not like higher costs, I commend the agency for absorbing part of the increase through improved efficiencies. FGIS has responded to industry in this case.

FGIS must, by Executive Order, negotiate any change in work procedures with its union representatives. This has made needed changes that would improve operations and flexibility very difficult to achieve. The grain trade is dynamic and ever-changing and needs flexibility to compete.

3. I have stated that FGIS has communicated well with the grain trade; but I think there is room for improvement. One area would be to improve communication concerning research that FGIS is contemplating conducting. I think a research committee or subcommittee of an already existing format could do the job, without forming a new committee. This would help bring more focus to research and help ensure that scarce research funds are well spent.

4. I think the Congress and the Executive Branch need to better understand this agency's multiple functions and the funding that supports FGIS activities. As I have stated, this agency has a dual function: 1) act as a direct service provider that is necessary to the conduct of a very large export trade; and 2) serve as the "keeper of the standards" for U.S. grains. It is an agency that provides many services, not directly related to the daily export of grain, as noted earlier in this testimony. It is more of a broad oversight regulatory authority. The cost for this oversight should be borne by all segments of the industry.

GIPSA/FGIS is funded by two methods:

1. User Fees
2. Appropriated Funds

In that context, the exporters understand that we must pay for the direct service or supervision and an appropriate amount of overhead to support it. But as an agency with many functions other than grading grain for export, GIPSA/ FGIS benefits all sectors of the U.S. grain production and processing system as well as consumers. Therefore it is

critical that appropriated funds or some other funding mechanism are readily available for this support. The U.S. exporter cannot continue to shoulder more in user fees than its fair share. Each budget cycle we face this pressure to shift more costs to user fees which are paid primarily by exporters. It is easy to see exporters as a funding source since we are mandated users of the service.

The economics of GIPSA/FGIS are much like that of the grain industry. This is a volume oriented business that has very identifiable breakeven volume numbers. It is not accident that the financial health of FGIS has improved as export volumes has risen for the past three years. The industry needs volume to survive.

5. The time line for changing procedures, regulations and practices needs to shrink to accommodate the faster pace of change in business. The Federal system is slow and cumbersome, depending on the change sought. This is an issue that has been discussed with the agency but I feel it needs to be highlighted today. If the Federal system is to be a reliable business partner, it needs to move faster and we need to anticipate change better.

The Future:

This is an exciting and challenging time for Agriculture. The advent of biotechnology holds much promise for the grain industry and great challenges also. Importers of U.S. grains are becoming much more sophisticated in the specifications that they demand from U.S. grains.

In the future GIPSA needs to work closely with all segments of the grain industry to:

1. Be prepared to provide GMO trait testing as the market may require.

2. Identify and provide the testing of end use value characteristics that processors require and producers need to know.

3. Continue the development of technology that lowers costs and improves delivery of services and data.

4. Identify how GIPSA/FGIS fits into the E-commerce economy.

5. Continue to identify and conduct research that benefits the producer, consumer and the grain handling and processing industry.

6. Have more contact with grain importers to increase FGIS understanding of importer concerns and requirements.

I will conclude by saying the export industry needs GIPSA/FGIS to be a cost effective, forward-looking business partner that assists U.S. producers and exporters in expanding our world market share. FGIS is a critical link in the conduct of the U.S. export grain trade.

That concludes my testimony, Mr. Chairman. I will be happy to answer any questions.

January 2000

BIOGRAPHY

Bert Farrish
4305 S.W. Tunnelwood St.
Portland, Oregon 97221

PROFESSIONAL BACKGROUND:

- o 1973-1977 Cook Industries, Inc.
- o 1977 Farmer's Export Company
- o 1977-1979 Farmer's River Terminal of Louisiana, Inc.
  General Manager
- o 1979-1996 Columbia Grain, Inc.
  Superintendent, Vice President, Senior Vice President
- o 1996- President, Columbia Grain, Inc.

INDUSTRY-COMMUNITY INVOLVEMENT:

- o Board of Directors, Louisiana Grain and Feed Assoc.
  - 1979
- o Grain Elevator and Processing Society
  - 1989-1994 International Director
  - 1994-- International Treasurer
  - 1989-1994 Founded and Chaired GEAPS Rail Car Task Force
  - 1991 Member of Distinction award winner
- o Member- PNITA (Pacific Northwest International Trade Assoc.)
- O 1994-1996 Commissioner-Oregon Grains Commission
- o 1994-1996 Board Member, U.S. Grains Council
- o 1996- North American Export Grain Association; Grades and Inspections Committee member. Chairman 1999-
  March 1999-Represented NAEGA in TCK negotiations with China
  Sept. 1999- NAEGA Board of Directors
  Dec. 1999-NAEGA Delegate to Seattle WTO

1999-NAEGA Representative to Grain Quality Workshop

- O 1997-Chairman-Lead Negotiator for Pacific Northwest Export Grain operators; contract negotiations with ILWU
- O 1997- 2000- Federal Grain Inspection Service Advisory Committee
- O 1997-1998 Board of Directors, Lewis & Clark Chapter, March of Dimes
- O 1995-1998- Jesuit High School Auction Committee
- O 1998- Columbia River Channel Coalition, Leadership Advisory Committee
- O 1998- U.S.Senator Gordon Smith, County Council member

PERSONAL BACKGROUND:

- o Born October 8, 1950, Greenwood, Mississippi
- o B.S. Mississippi State Univ. College of Agriculture
- o U.S. Army Reserves 8 years; Captain U.S. Army Corps of Engineers.

Statement of the

National Grain and Feed Association

Before the

Committee on Agriculture, Nutrition and Forestry

U.S. Senate

February 1, 2000

Presented by Robert Smigelski

The National Grain and Feed Association appreciates the opportunity to submit this statement on the Grain Inspection, Packers and Stockyards Administration (GIPSA). Specifically, we will provide comments on the program within GIPSA known as the Federal Grain Inspection Service (FGIS). The FGIS administers the U.S. Grain Standards Act (USGSA) and provides official inspection services to NGFA members. The industry values the credibility and integrity of the official inspection system and believes it provides benefits to U.S. agriculture in domestic and international markets. We note that the number of complaints on the quality of U.S. grades on export shipments by foreign buyers has declined in recent years.

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.

The FGIS has changed in many ways since Congress authorized it in 1976. These changes include a dramatic downsizing of the Agency in the early 1980's and in 1994 a merger with the Packers and Stockyards Administration (PSA) to form the Grain Inspection, Packers and Stockyards Administration. FGIS is largely a service agency to the commercial grain sector. User fees paid by exporters and domestic commercial shippers and receivers fund approximately 75% of Agency operations.

The FGIS and industry maintain a positive working relationship. Agency management routinely meets with NGFA and its Grain Grades and Weights Committee to discuss issues affecting the official system. In 1998, the FGIS announced a strategic plan that, in part, seeks to "increase the efficiency of U.S. grain marketing… to streamline grain inspection and weighing" and "provide … cost-effective … grain inspection and weighing services." We are supportive of these goals

but remain concerned that FGIS may lack sufficient managerial flexibility to fully achieve them. On the other hand, the Agency has been working with industry to improve automation at export facilities, an effort we applaud.

The Agency was last re-authorized in 1993 for seven years. Thus, by September 30, 2000, Congress must re-authorize several provisions of the USGSA to allow FGIS to continue providing official services. These provisions include collection of fees for official inspection and weighing activities, the 40% cap on administrative and supervisory costs and the authority for the FGIS Advisory Committee. The 2000 Agency re-authorization provides an opportunity for industry and Congress to consider what changes may be needed in the official inspection system to ensure it can continue to meet the needs of the marketplace.

In this regard, we would like to share our perspective on several issues affecting the official system. Several of these issues are not new having been shared with FGIS management and Congress in the past.

The Operating and Cost Structure of the

Domestic and Export Official System Markets

The cost of the official system in domestic and export markets remains a concern to NGFA members.

· Domestic Markets: Official inspection and weighing of U.S. grain in domestic commerce are performed upon request by private agencies granted an exclusive license by FGIS to perform official services in a particular area. In 1993, the GAO study found that the use of the official system in the interior markets has declined because of high costs, inflexible service, consolidation within the industry, and increasing acceptance of unofficial and in-house grades by the market. While it appears that utilization of the domestic official system may have stabilized somewhat in recent years, a 1999 survey of NGFA members indicates that cost of service remains a strong concern.

As a result of the GAO survey, the NGFA recommended during the 1993 re-authorization of the Agency that Congress require FGIS to conduct pilot programs to open selected interior official territories to competitive bidding for services. The Agency began a series of pilot programs in 1995 and the results indicate that granting FGIS permanent authority to allow increased competition within the domestic official system may be beneficial.

· Export Markets: The U.S. Grain Standards Act (USGSA) requires that export grain be officially inspected and weighed by FGIS personnel. Over the past 10 years, the FGIS has experienced significant financial losses, seriously depleting the Agency's financial reserves. As a result, the FGIS has instituted a series of fee increases over the last several years that has resulted in making the cost of official inspection one of the top operating expenses at export elevators. While the Agency reported approximately $1.8 million in profits at the end of Fiscal Year 1999, the cost of official inspections at export locations and future management of those costs remains a concern. We believe managerial that both FGIS and industry would benefit if FGIS management had additional flexibility to control costs and maximize operating efficiency.

On February 2, 2000, the NGFA's Grain Grades and Weights Committee will meet to discuss a number of policy options to assist FGIS efforts in fulfilling its role under the USGSA. One option under serious consideration by NGFA would shift FGIS from a more traditional government agency model to a Performance Based Organization (PBO) within government. The PBO concept was designed as a business model for government agencies heavily focused on service to the private sector, a description that fits much of FGIS operations as well. The PBO concept has been used successfully in the federal government's Student Financial Aid.

While several questions remain, we believe the PBO concept is attractive because it may offer FGIS greater flexibility in the way its manages its operations while retaining strong federal government oversight of the inspection functions. To move forward with this concept would require authorizing legislation. NGFA's committee will be studying the pros and cons of this concept and decide whether to make a formal legislative proposal shortly.

Another policy option that should be considered is reducing 40% cap on administrative and supervisory fees to 20%. Reducing the 40% cap would be consistent with trends within private industry. Furthermore, the Agency reported in 1995 that administrative and supervisory costs represented 23% of total program costs. Thus, a reduction to 20% may also be consistent with trends within the Agency itself.

FGIS Advisory Committee

The FGIS Advisory Committee was created to provide advice to the FGIS Administrator on implementation of the USGSA. Over the years, the direct users of the official inspection system - those actually paying for the service - have increasingly come to question the relevancy of the FGIS Advisory Committee to assisting the Agency in its responsibilities. We think a stronger representation by direct users on the Advisory Committee would help address this situation and recommend that Congress authorize that that at least 10 of the 15 advisory committee members represent companies that are direct users of the official system.

Testimony of

Mr. Mike Clark
Vice President
Illinois Corn Growers Association

On the behalf of

American Soybean Association
National Association of Wheat Growers
National Corn Growers Association

Before the

Senate Committee on Agriculture, Nutrition and Forestry

February 1, 2000

Mr. Chairman, members of the committee. I am Mike Clark, and I currently serve as Vice President of the Illinois Corn Growers Association. I raise corn, soybeans and wheat near Homer, Illinois, and Vedersburg, Indiana.

It is my honor to appear before you this morning on the behalf of the American Soybean Association, National Association of Wheat Growers and National Corn Growers Association. Together, these three national organizations represent a significant amount of U.S. agricultural production and the vast majority of grain producers.

I would first like to thank the Committee for holding this hearing. As a farmer, my operation is directly impacted by the work of the Grain Inspection, Packers and Stockyards Administration (GIPSA) and the grain standards it enforces.

As we enter the new century, we should take the time to review how our government operates and ask ourselves: Is there a better way? This certainly applies to GIPSA and the standards it enforces. Indeed, many of the grain standards are nearly a century old themselves, having been created by the Grain Standards Act of 1916.

While GIPSA is to be commended for its efforts in modernizing its operation, little has been done to bring grain standards into the twenty-first century. As you well know, U.S. producers must export a significant portion of their crop each year to remain solvent. This requires us to compete on a world market against well-positioned competitors. Across the globe, world grain buyers have grown more sophisticated in their buying requirements. Yet, we continue to rely on standards that largely only describe external characteristics.

Current U.S. grain standards measure only volume and outward appearance. Very few inspection standards exist to give grain buyers the information they really want: the end-use characteristics of the crop. Farm groups, this committee and the agency need to engage in open dialogue to determine if these needs are to be meet by the public or private sector.

Take for example how we measure protein in wheat. While wheat is graded by the amount of protein it contains, no standards are available to measure the quality of the protein or the gluten content. Tests and standards need to be developed to identify the inherent traits that bring about the highest end-use value and help identify and preserve true wheat quality.

Millers and bakers want to know how the wheat they purchase will grind into flour; how it will bake into bread; and how it will effect the quality of their product. Without making changes which reflect end-use quality, U.S. grain producers will be left flat-footed on the world market, unable to capture the true value of their product.

To its credit, GIPSA has made some advances in this area. However, much remains to be done. We need to harness the continued advances being made in technology to bring about a reliable and quick test that will predict the intrinsic qualities desired by the end-user. In addition, we must retain the flexibility to adapt such standards as new technologies are developed.

These issues are made even more complex when we consider the growth of biotechnology. For example, consider for a moment how biotechnology is currently effecting the corn industry.

Biotechnology is clearly the single largest driver of change for the corn industry, as such it will be important for all segments of the industry – producer, processor and regulator – to define their new and different role in this era. The rate of change spurred by biotechnology is so rapid that we cannot rely upon the time-tested practice of defining

policies based upon the experience of the past, but rather by anticipating the needs of the future. We are still defining our regulatory expectations of GIPSA and other government agencies in that future. We do anticipate that in the future the opportunities for corn farmers to extract additional value from the crop will arise from being able to move up and down the value chain. This means we will need to better know and identify the intrinsic qualities of an increasingly segmented corn market – a market place where farmers, handlers, processors and customers will be tracking, testing and identity preserving individual load lots of grain as it moves through the value chain.

In this new arena, standardization of tests and testing equipment will be vital. GIPSA can play an important role in making sure that tests for intrinsic qualities are timely, repeatable, verifiable and of a nature that can be used by commerce in our country elevator system. To extract value from a new era of biotechnology, we will need standardized tests that confirm that value.

Likewise, the soybean industry is actively considering the development of testing and analytical procedures for a variety of traits derived through both commercial breeding and biotechnology. These traits include high content levels of oleic and stearate fatty acids, low linolenic acid content, low phytate content, and high sucrose content. Soybean growers are working with other industry partners to develop standards for these characteristics for recommendation to GIPSA.

The impact of biotechnology on the grain trade and in turn our expectations of GIPSA is currently evolving. We are still exploring our expectations of contracts, grades and standards in the future. While we cannot say today with certainty our expectations for GIPSA in the future, we look forward to dialogue with the agency and this committee to clarify that role.

Meanwhile, we must continue to monitor and improve GIPSA's everyday operations and the grain standards we currently have. It is vitally important that, in addition to the current user fee system, GIPSA continue to be funded by both appropriated federal funds.

The standardization and development of tests, as well as other related GIPSA activities, benefit society at large and should be funded by society rather than through user fees.

Just this year, GIPSA developed standards for a new class of wheat: hard white. It is to be commended for working with wheat producers and commissions from across the country to develop reliable, workable standards that will help guide the development of this class of wheat across the mid-west.

While not all producer groups are in agreement, the National Association of Wheat Growers commends GIPSA and its partners at the Foreign Agricultural Service for their efforts in advancing USDA's grain cleaning initiative. Just last week, representatives from several state wheat commissions joined grain exporters, foreign grain buyers and grain millers from around the globe in providing comment on the need to improve our grain cleaning capabilities for grain sold through the Gulf of Mexico.

As I mentioned earlier, our customers around the world continue to demand clean, high quality grain. The implementation of the USDA wheat cleaning initiative would be a solid first step towards regaining our competitiveness in the world grain market.

Again, Mr. Chairman, let me thank you and the Committee for the opportunity to appear before you today. I appreciate your timely evaluation of these concerns and welcome any questions you might have.

STATEMENT OF

MR. DENNIS WIESE
PRESIDENT
SOUTH DAKOTA FARMERS UNION

ON BEHALF OF THE

NATIONAL FARMERS UNION

BEFORE THE

SENATE AGRICULTURE, NUTRITION AND
FORESTRY COMMITTEE

FEBRUARY 1, 2000

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STATEMENT OF
MR. DENNIS WIESE, PRESIDENT
SOUTH DAKOTA FARMERS UNION
ON BEHALF OF THE
NATIONAL FARMERS UNION
BEFORE THE
SENATE AGRICULTURE, NUTRITION AND FORESTRY COMMITTEE
FEBRUARY 1, 2000

Mr. Chairman, Members of the Senate Agriculture, Nutrition and Forestry Committee, my name is Dennis Wiese. I serve as president of the South Dakota Farmers Union and member of the board of directors of the National Farmers Union. It is an honor to appear before this committee representing the 300,000 family farmer and rancher members of the National Farmers Union to offer our views concerning concentration within agriculture and important aspects of the Grain Inspection, Packers and Stockyards Administration (GIPSA). GIPSA has two primary responsibilities: the Packers and Stockyards Programs and the Federal Grain Inspection Service (FGIS).

Packers and Stockyards Administration

The Packers and Stockyards Administration of GIPSA is responsible for overseeing market competition in the livestock sector. In recent years, the levels of vertical integration and captive supply have grown rapidly and are major concerns for producers seeking competitive markets. Farmers and ranchers believe stepped-up enforcement of the Packers and Stockyards Act is key to restoring adequate levels of market competition necessary to maintain an independent producer livestock sector.

National Farmers Union supports a number of changes to improve the functioning of the Packers and Stockyards Administration. First, its authority should be expanded to include the poultry industry and livestock feedlots. Department of Agriculture attorneys should be allowed to try cases before the federal courts in addition to their current authority within the administrative court system. Funding for the Packers and Stockyards Administration should be increased to provide additional resources for investigation and enforcement. Violators of the Act should be liable for both compensatory and punitive damages.

In addition to modifications affecting the execution of the Act, Congress should establish a specific level of concentration within a sector or region that would automatically constitute an anti-competitive practice in violation of the Packers and Stockyards Act. Finally, Congress should prohibit packer ownership of livestock that provides direct market competition with independent producers, while adopting appropriate provisions to allow the formation and operation of producer-owned cooperatives.

In 1999, Congress approved legislation mandating that livestock prices be reported to increase the transparency and competitiveness in those markets. We applaud

that effort, and urge continued oversight by the Congress as the Department of Agriculture implements the price reporting program.

Federal Grain Inspection Service

The Federal Grain Inspection Service has the responsibility to provide both official and unofficial grades for U.S. grain commodities sold into the domestic and export markets based on standards adopted by the agency. These standards provide the foundation for determining specified quality, cleanliness and intrinsic characteristics that are a component of U.S. grain sales contracts. In the absence of an appeal, FGIS grades become the basis for determining adjustments to the final settlement of sales agreements between farmers and merchandisers, and in transactions between the merchandising sector and domestic processors and overseas customers.

In order to ensure objectivity and accuracy in fulfilling this mission, FGIS engages in research and development activities to review and test new procedures, standards and technology, provides on-going education for inspectors, and engages in monitoring its performance and output against other grain inspection systems

A user fee system, that is periodically modified, has been established to recover a significant portion of the cost of the services provided by the FGIS. However, as with the majority of the marketing expenses associated with the grain sector, the grain producer directly or indirectly pays the cost of inspection services through adjustments to the price received at the farm-gate. The farmer thus has a strong vested interest in an efficiently run agency that adopts, consistently applies and enforces standards that enhance the marketability and competitiveness of U.S. grains to achieve the highest level of consumer satisfaction.

In the new decade, significant economic challenges confront grain producers that are related to the mission of the Federal Grain Inspection Service. These challenges include the traditional issues of agency service levels, modifications to standards, dispute settlement and user fees. In addition, FGIS must adapt to emerging considerations that are the result of increased competition for markets and market share. These issues include grain cleaning and new production and product technologies.

The issue of grain cleaning takes on new significance in a global market where many forms of intervention have been reduced that, in the past, have been used to offset market advantages associated with large-scale commodity cleaning requirements and operations. In addition, the increased market power associated with highly concentrated and integrated multinational merchandising and processing sectors allows these companies to play differing national marketing systems, i.e. those that require grain to be cleaned versus those that do not, against one another to the disadvantage of grain producers globally.

For example, the wheat marketing system in western Canada is dominated by a monopoly wheat board that has historically mandated that all wheat destined for overseas

delivery be cleaned before shipment and that a high level of segregation by various characteristics be maintained from the farm through the export position. This has allowed Canada to claim a reputation, as a consistent supplier of higher quality wheat than is available from the U.S. even though both countries raise the same classes of the commodity and the same multinational merchandisers may ultimately market the wheat. When coupled with a differential pricing capacity, Canada claims it is able to gain premium prices in enough markets to outweigh the cost of cleaning. It may also provide a product that exceeds contract specifications, develops a high level of customer loyalty, maintains overall price competitiveness globally and produces higher market returns to its producers.

In the U.S., the wheat marketing system is based on meeting the minimum sales contract specifications. This is accomplished by blending of lower grades of wheat for which the merchandiser paid a discounted price to the producer with higher grades that generally do not receive a premium except in the case of protein levels. While the system is effective in creating a market for all grade levels at nearly all times, our reputation as a supplier of quality wheat suffers even when the number of complaints about grain shipments that fail to meet contract specifications is low.

For a period of time, the U.S. was able to utilize price discounts through export subsidies to offset a competitive quality disadvantage through the Export Enhancement Program (EEP) and other sales incentives. Ratification of the World Trade Organization created commitments to reduce and/or eliminate many of these programs.

We believe the U.S. should utilize a portion of the budget savings associated with those reductions to implement a grain cleaning pilot program to test the effectiveness of such a system, including its customer relation's impact.

Some may view this approach as an unnecessary and undesirable intervention on the part of government that is not supported by the marketplace. However many of those same opponents directly benefit from the business generated by the Canadian system and/or creates additional company profits by blending various grades of U.S. grains that have been purchased from the producer at a discount.

For the grain inspection service, wide-scale grain cleaning could potentially streamline the grading process, increase service efficiency and allow more focus on other difficult grading and inspection issues while lowering the cost of grain inspection to the producer.

Similarly, new technologies such as genetic manipulation of grain crops to achieve specific production and/or physical attributes raise serious grain inspection issues. These include certification as to the presence or absence of genetically modified organisms, product segregation, and the potential for, and vesting of liability in the event of miss-identification of bio-engineered crops.

Unless and until all nations reach agreement on the conditions of acceptance of these crops, and cost-effective, efficient testing procedures are developed consistent with such an agreement, regulatory agencies and producers will remain at risk. The FGIS in its certification role will be challenged in terms of its credibility. U.S. crop producers will ultimately bear the market risk of the technology through the imposition of domestic and international market barriers, price discounts and potential legal liability. The majority of economic benefits associated with biotechnology will flow to those with the greatest level of multinational integration and market power that can dictate the terms of both production and marketing.

We support Congressional action to ensure that producers of genetically enhanced agricultural products are held harmless from any legal liability that may result from the production or marketing of these products, and that producers should not be responsible for cost of any testing requirements that may be imposed. In addition, we support cooperative international efforts to ensure consumer confidence in the agricultural products they purchase, including the establishment of a labeling requirement to allow consumers the ability to make informed purchasing decisions. Finally, the market for genetically modified products is likely to require a much better system product segregation that currently exists in the U.S. We believe that USDA should implement an on-farm grain storage facility loan program and limited farmer owned reserve program. These initiatives would help ensure that adequate infrastructure exists to provide the level of identity preservation and stock diversity necessary to obtain the maximum market and production flexibility from these products.

Conclusion

In conclusion, the National Farmers Union supports changes to the Packers and Stockyards Act that expand administrative authority in both scope and litigation capacity, establishes punitive and compensatory liability for violators and ensures adequate funding for investigation and enforcement. Furthermore, Congress should establish a concentration threshold that would constitute anti-competitive practices in violation of the Act. In addition, we urge Congress to prohibit packer ownership of livestock in direct competition with independent producers.

Concerning the Federal Grain Inspection Service, the National Farmers Union seeks to ensure an objective and efficient grain inspection system. The system must be capable of addressing the traditional issues of service levels, grading standards, user fees and dispute resolution while also meeting new challenges and opportunities such as grain cleaning and the many issues concerning the production and marketing of genetically modified crops.

We support a pilot program to encourage the commercial cleaning of grain to meet customer needs and the competitive challenges faced by the grain industry. Furthermore, we believe Congress, USDA and the Federal Grain Inspection Service must address the issue of genetically modified crops in a way that reduces the market, financial and legal risk for producers and ensures consumer confidence in both our regulatory

system and the agricultural products we place on the market. Specifically, we believe producers should not be financially liable for testing or future production and marketing consequences of GMO production. In addition, we support federal programs that will assist in the segregation of GMO and non-GMO production through a grain storage facility loan program and a farmer-owned reserve.

Mr. Chairman, on behalf of the members of the National Farmers Union, I thank you for the opportunity to share these thoughts with the committee today, and will respond to any questions at the appropriate time.

DOCUMENTS SUBMITTED FOR THE RECORD

FEBRUARY 1, 2000

JERRY JEROME, *Chairman*
NICK WEAVER, *Vice Chairman &*
Secretary-Treasurer
STUART E. PROCTOR, JR., *President*

STATEMENT OF

THE NATIONAL TURKEY FEDERATION

to the

SENATE AGRICULTURE COMMITTEE

Hearing on the Authority of the
Grain Inspection, Packers and Stockyards Administration

February 1, 2000

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Introduction

The National Turkey Federation (NTF) appreciates the opportunity to submit this statement for the record at today's hearing on the contract enforcement authority of the Grain Inspection, Packers and Stockyards Administration (GIPSA). NTF represents virtually all U.S. turkey processors, as well as turkey growers, breeders and hatchery owners, and allied industry. NTF is the only national trade association representing the turkey industry exclusively, and we believe we have a unique perspective to add to the discussion of what authority the GIPSA should have to enforce its regulations regarding weighing practices and contract compliance.

Current law requires GIPSA to enforce these regulations through the federal courts. The Secretary of Agriculture, beginning with the 1997 report of his "concentration commission", has raised questions about whether this enforcement process is too cumbersome and prevents violations from being halted and punished. This Congress, legislation has been introduced in the House to allow GIPSA to use administrative civil penalties to enforce its weighing and contract compliance provisions. NTF also understands that similar provisions may be included in Senate legislation designed to address a variety of industry structure issues.

NTF at this time is neutral with regard to this legislation, and the federation's members encourage Congress to remain neutral on the issue until GIPSA answers several important questions to justify the proposal to enhance its enforcement authority.

Need for New Authority Unclear

The concentration commission, GIPSA and other supporters of enhanced enforcement make two distinct arguments in favor of the proposal. One is that GIPSA already has such

enforcement authority for livestock transactions and that it is only natural that the authority should be extended to poultry. The second is that the Justice Department doesn't have the time or resources to enforce alleged poultry processor violations of the weighing and contract compliance regulations and, as a result, these alleged violations go unpunished.

It is relatively easy to find the flaws with the first argument. The existence of one set of compliance mechanisms in livestock does not mean identical mechanisms are appropriate for poultry. We don't apply processing rules governing the de-feathering of poultry to cattle, and we don't apply the rules for removing cows' hides to poultry. The structures of the livestock and poultry industries are significantly different. For example, an individual herd of cattle can be the subject of numerous sales transactions involving many different parties before finally reaching the processing plant. A different set of enforcement tools may be necessary to govern such complex transactions than are necessary to govern the poultry industry, where birds typically have only one owner – the processor – throughout their growing cycle.

The second argument is the one that goes to the heart of NTF's concerns about this issue. GIPSA and supporters of enhanced enforcement say serious violations are going unpunished because it is difficult, if not impossible, to enforce the provisions through the Justice Department and the courts. The implied argument is that GIPSA's lack of civil penalty authority for these poultry regulations is a congressional oversight that can be easily corrected.

It is important to understand that the lack of civil penalty authority is not an oversight at all. Congress in 1987 passed the Poultry Producers Financial Protection Act (P.L. 100-173), which clarified several aspects of GIPSA's authority over the poultry industry. The legislation made clear that GIPSA retains full regulatory authority over transactions involving live poultry and

that the Federal Trade Commission has full regulatory authority over transactions involving processed poultry. The bill also extended the Packers and Stockyard Act's statutory trust and prompt payment provisions to the poultry industry.

At the time, Congress debated fully the question of whether to give the agency civil enforcement authority for weighing and contract compliance regulations, as they applied to poultry. This debate involved the members of the House and Senate committees of jurisdiction, representatives of the national poultry trade associations and representatives of poultry growers. Part of the consensus agreement that came from these debates was that there was no need to grant GIPSA the civil penalty authority. In the report accompanying the House version of the bill, Congress speaks affirmatively to the issue, saying: ***". . . jurisdiction over live poultry transactions (i.e. weighing practices and contract compliance) will remain with the Packers and Stockyards Administration . . . Further, the Packers and Stockyards Administration must continue to enforce these provisions of the Act through the U.S. District Courts."***

Forty-four members of the House Agriculture Committee, including the current Agriculture Secretary, were cosponsors of this compromise bill, and the legislation passed both chambers without dissent.

So, the relevant question for the Committee and Congress to ask is: what has changed since 1987 that would necessitate reversing the policy established in the Poultry Producers Financial Protection Act? If there have been rampant violations of GIPSA's weighing and contract compliance regulations, and these violations have gone unenforced by an overworked, understaffed Justice Department, then a new law may be in order. But, giving any regulatory

agency additional regulatory authority without first identifying a problem that needs regulating would set a very dangerous precedent.

NTF believes GIPSA to this point has not provided sufficient information to answer these questions, and until that information is provided, it is difficult to see how Congress can make a decision on the need for enhanced enforcement authority.

Simple Questions, Simple Answers

NTF has begun what it hopes will be a relatively quick process of gathering the information necessary to determine its own policy toward GIPSA's request for enhanced enforcement authority. We recently wrote GIPSA administrator James R. Baker and posed three simple questions to the agency. We asked:

- how many complaints GIPSA has received from turkey producers since 1987;
- how many of these complaints were referred to the Justice Department; and
- how many of these referrals were not prosecuted by the Justice Department and the reasons it did not pursue these cases?

We believe it will be easy for GIPSA to answer these questions, and we believe the answers to these questions will tell us all we need to know about whether GIPSA needs this authority to correct any problems in the turkey industry. We strongly encourage this Committee to join NTF in seeking answers to these questions from GIPSA because they will form a solid foundation for determining the need for future legislative action.

Conclusion

NTF's members have a basic philosophy that applies to almost any policy area. They are strongly opposed to expanding federal authority into that area unless it can be demonstrated clearly that a problem exists and that only federal intervention can address the problem. NTF remains neutral toward proposals to enhance GIPSA's enforcement authority because a problem with weighing practices and contract compliance has been alleged, but not yet proven.

We hope GIPSA can provide clear, indisputable evidence at the earliest possible date as to the nature and extent of any problems that exist in the poultry industry. Until then, we urge Congress to join NTF in remaining neutral toward legislation that would enhance GIPSA's enforcement authority with respect to weighing practices and contract compliance in the poultry industry.

NTF would be happy to answer any questions the committee may have.

Structural Change and Market Performance in Agriculture: Critical Issues and Concerns about Concentration in the Pork Industry

by
Philip Paarlberg, Michael Boehlje, Kenneth Foster, Otto Doering, Wallace Tyner

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STRUCTURAL CHANGE AND MARKET PERFORMANCE IN AGRICULTURE: CRITICAL ISSUES AND CONCERNS ABOUT CONCENTRATION IN THE PORK INDUSTRY
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Abstract

We have witnessed profound changes in the pork sector over the last several years. These involve integration and concentration that raise issues of competitiveness in both input and product markets as well as issues of who bears risk and who reaps rewards. We see clear evidence of increased concentration, by several measures, to the point where public vigilance is warranted. Two major policy options are anti-trust action and increasing the market power of hog producers through institutional arrangements new to the hog industry. Better information in specific areas of concern is needed before informed public policy can be made with respect to either policy option, and the option of increasing producer market power will require active public support.

Keywords: Pork industry, public policy, pricing, concentration, market power, vertical integration.

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Structural Change and Market Performance in Agriculture: Critical Issues and Concerns about Concentration in the Pork Industry.

by
Philip Paarlberg, Michael Boehlje, Kenneth Foster, Otto Doering, and Wallace Tyner

U.S. agriculture is in the midst of major structural change – changes in product characteristics, in worldwide production and consumption, in technology, in size of operation, and in geographic location. Production is changing from an industry dominated by family-based, small-scale, relatively independent firms to one of larger firms that are more tightly aligned across the production and distribution chains. The sector is becoming more industrialized, more specialized, more integrated, more managerially intense, and the pace of change is increasing.

Agricultural Sector Issues

Competitiveness of product and input markets

The development of tighter linkages in the food production and distribution industries may have a major impact on market access in both the input and product markets. The development of larger scale firms raises questions about concentration and oligopolistic if not monopoly power in negotiating terms of exchange.

- How will the structural changes in agriculture impact access to product and input markets?
- Do we now have markets in contracts rather than products or inputs?
- What are the implications for producers, consumers and competitive markets? More specifically, is concentration in the poultry, pork and beef industries sufficiently high to warrant antitrust or other government intervention?
- What are the consequences of such intervention (or of not intervening) in terms of incentives to innovate, efficiency, externalities and the distribution of returns and risks?
- And what are the intervention alternatives? Should we restrict consolidation in buyers and sellers, or should we encourage producers to develop networks and alliances to negotiate from a position of more economic power than would occur otherwise.

Captive suppliers and other forms of vertical integration and coordination are potentially detrimental to both competition and price discovery. The degree to which these effects occur varies by region and time of the year. These arrangements have a tendency to thin market price reporting (reduce the volumes on which reported prices are based) and shorten the weekly marketing "window," which can disadvantage suppliers who do not have a packer arrangement. Further, they distort reported market prices downward. It is widely agreed that equal and accurate market information improves the price discovery and determination process. Poor information can lead to unnecessary price volatility or slow adjustment to changing supply and demand conditions. Inadequate or uneven information can cause some market players to be disadvantaged relative to others, and price levels could be biased for an extended period.

Risk and value chains

Who bears the risk and captures the reward in the increasingly more tightly aligned food chain? The common perception is that vertical linkages or alliances through ownership or contract production will reduce price, quality and quantity risk. But the implications for financial and strategic risk are less clear. The dispersion and/or concentration of financial risk as one moves from independent firms to vertical linkages is a critical issue that merits detailed analysis from a policy perspective.

Tighter alliances in the food chain are likely to reallocate the risk and uncertainty relative to accurate messages concerning prices, quantities and qualities of products and attributes. Messaging is likely more precise, timely, and generally more accurate for participants in the chain than might be provided by market forms of coordination. But what about the risk faced by those who are not part of the tightly aligned supply chain – i.e., are not qualified suppliers? Is there more volatility in the prices they receive because of thin markets? Do they have access to a market, or are they closed out because only qualified suppliers can participate? If those who cannot participate in the qualified supplier systems can only sell in commodity markets, and these markets take on the characteristics of a salvage market, do those left out incur more of the risk of more tightly aligned chains without the potential of receiving any of the rewards? If markets become sufficiently concentrated that only one or possibly two qualified supplier arrangements are available in a particular locale, how can the participants even be assured that their share of the risk and rewards of participation are equitable? The fundamental issues of access to information, transaction transparency, equitable sharing of risk and rewards by nonparticipants as well as participants in tightly aligned supply chains, and the risk associated with market access are all important market risk and performance issues.

Privatization of intellectual property and innovation

The agricultural sector is confronted with new questions like: What role does intellectual property rights law play in encouraging more tightly aligned supply chains and monopoly or oligopoly power? How does the privatization of research and development (R&D) and information markets impact the distribution of the benefits of innovations, the rate of innovation, access to markets, and the competitive rivalry in markets? How important are property rights and rent-seeking behavior in encouraging firm growth or in stimulating economic development?

As more and more of the R&D effort, and thus new innovations, come from private sector firms rather than traditional public sector sources, and as more of the information dissemination system becomes privatized, individual firms have more potential to capture value from intellectual property. They have the potential to restrict access to new ideas and information to particular users, thus favoring some and excluding others from the ideas, technology or information necessary for them to be competitive. Initial concepts of intellectual property rights, including patent and copyright law as applied to agriculture, were developed in an era of domestic markets and national firms; a relatively large public sector research, development and information dissemination system; and a limited role of information as a critical resource. Rules of the game have changed, and concepts may need to be reevaluated in the context of global markets and multi-national business firms; the shrinking role of the public

sector in research, development and disseminating information; and the increasing importance of information compared to other resources as a source of strategic competitive advantage.

Concentration Issues For The Pork Industry

Evidence of increased concentration in hog slaughter

Like many industries, the hog slaughter industry is characterized by a small number of firms producing most of the pork, and a fringe group consisting of a large number of small slaughtering firms contributing little to total pork supply. All standard measures of market concentration suggest that the hog slaughter (packing) industry has become more concentrated since 1985. Packing plant and firm numbers fell by 46 percent from 1985 to 1997. Concentration indices which give the percent of total slaughter accounted for by the top 4 and 8 firms have also risen. In 1985, the 4-firm concentration index was 32.2 and the 8-firm index was 50.8. By 1997, the indices had risen to 54.3 and 75.7, respectively. Traditional classification rules used by economists would label an industry with the 1997 concentration indices found for hog slaughter as a moderately concentrated industry. Another measure of industry concentration is the Herfindahl-Hirschman (HH) index, which is the sum of the squared market share of all firms. In the HH index the influence of firms with larger market shares is assigned a greater weight. The HH index for the hog slaughter industry has more than doubled between 1985 and 1997.

The Herfindahl-Hirschman index can be used to estimate the equivalent symmetric number of firms in an industry. That is, if instead of an observed industry with a few large firms and a host of little ones, all firms in an industry were the same size, how many would there be? This symmetric firm number gives a sense for how "competitive" an industry behaves overall. In the case of hog packing the symmetric firm number for 1985 is 22. That means the industry behaved as if there were 22 equal sized firms in 1985. This is a number sufficiently large enough to avoid most pricing distortions associated with oligopoly and oligopsony. By 1997, the symmetric firm number for hog packing had fallen to 10. There is no specific value that serves as the threshold where we can say serious pricing distortions due to market power arise. However, once an industry drops to a symmetric firm number of 10, concern is warranted.

Limited information for 1998 and 1999 suggests that increasing concentration continues. Calculation of the 4-firm concentration index shows an increase from 54.2 to 56.3 in 1998. Recently, Smithfield moved to acquire Murphy Farms and Tyson's hog operations. If completed, this will consolidate several of the largest players and further increase the captive supply.

Economic implications of increased concentration

While every industry has unique characteristics, economic theory offers some general conclusions about the factors affecting pricing under oligopoly and oligopsony (imperfect competition). Economic theory for perfectly competitive markets gives straightforward predictions, but the conclusions under imperfect competition are unclear and depend on the interaction of several factors which determine pricing rules for outputs and inputs.

One factor affecting pricing is the nature of the strategic interaction among firms. That means, how a firm expects its rivals to react when its behavior changes. Do firms determine

price or output quantity? Do rivals match a firm's price change or not? Is one firm dominant and leads the industry while other firms act as followers? A related issue is whether the goods produced by different firms are different or alike. If the goods are different, firms are more able to compete on a price basis. If goods are the same, quantity competition seems more plausible. The extent of product differentiation is linked to the issue of price elasticity facing a firm -- that is, the extent to which demand changes as price changes. Under perfect competition, the demand facing a firm is perfectly elastic and a single firm cannot itself affect the price. Under imperfect competition that is not the case. The firm recognizes that it can affect the price and/or its rivals' behavior and uses that information in its decisions. More elasticity in output and input markets reduces the ability of a firm to manipulate prices or outputs. If consumers are price sensitive or have substitutes available, firms' ability to drive up the price and hold their market is limited. International trade also affects the exercise of market power. A nation that cannot affect the world price must behave as a price taker if domestic and world prices are linked. Domestic firms with market power cannot raise their prices if they face either the threat of import competition or the loss of export markets to other nations when they raise their prices. Whether inputs are traded in international markets also affects the use of market power. An industry may take the output price as given, but use its market power in influencing the price of a non-traded input.

There is limited information on all these factors for the hog packing industry. There is evidence of product differentiation as hams, shoulders, bacon, and ribs are not perfect substitutes. Yet, the aggregate demand elasticity for pork is estimated to be high compared to other foods, and the elasticities for the various pork cuts should be even higher. In addition, the United States both imports and exports pork, and pork prices in the U.S. and the world appear integrated. Thus, it is likely that packers have limited market power for pricing their pork products. On the other hand, imports of live hogs for packers is not very large relative to slaughter. These features suggest an industry which sets slaughter and meat output with limited control over the pork price, but with potentially substantial influence over the live hog price paid to the producer of hogs.

The cost structure of an industry also affects pricing under imperfect competition. Does the industry have large fixed costs? Are there economies of scale, other barriers to entry, or capacity constraints at the firm or industry level? Large fixed costs and entry barriers limit potential competition and enhance market power, which results in higher product prices. Fixed capacity constrains the reaction of rival firms. This tends to result in higher prices as well. Economies of scale drive unit costs lower as output rises, and thus reduces firm numbers. These effects work in opposite directions. Falling unit costs lowers output prices if the mark up is constant, but falling firm numbers increases mark ups on output. The hog packing industry is perceived as having large fixed costs and economies of scale. (The argument is made that the Fall 1998 hog price collapse was partially due to industry capacity constraints.)

Vertical relationships between input suppliers and manufacturers become critical under imperfect competition. Vertical integration and coordination may occur for several reasons including stable supplies and quality control. They are methods that can be used to exercise market power and extract excess profits. In general, as vertical coordination in a market increases, volatility in spot markets increases because those markets become thinner. Spot markets become the buffer for vertically coordinated firms. Unanticipated rises in demand are met by purchases of inputs in spot markets. Unanticipated reductions in demand end up with

unwanted inputs dumped in spot markets.

There is evidence that increasingly large numbers of hogs move under direct ownership or contracts. As concentration and integration increases, problems of volatile spot markets and market foreclosure for independent growers are likely to increase. This was a concern in 1998 when the spot market was seen by some as having to absorb the full impact of excess supply and limited slaughter capacity. Thus, "independent" producers faced a precipitous price decline.

An illustration of what may be occuring

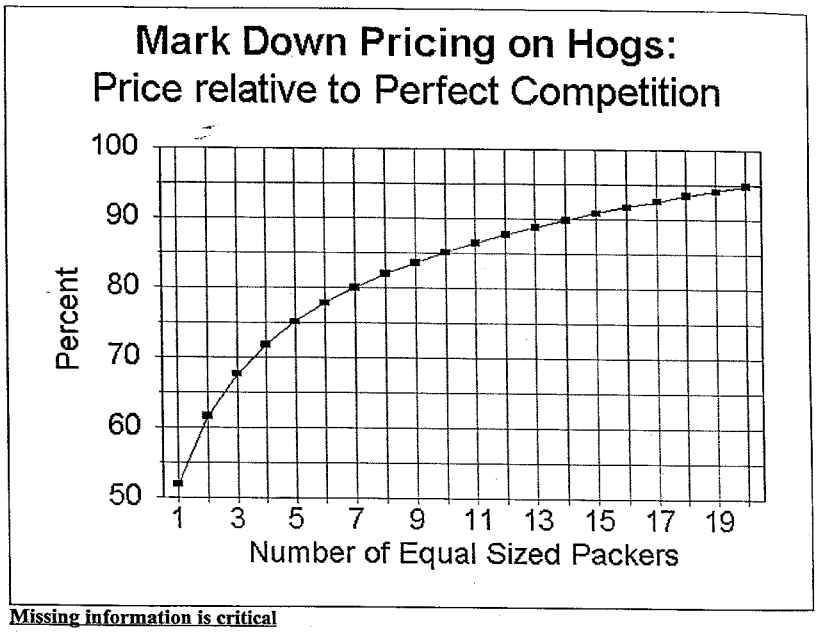
We constructed a model to illustrate how these factors of concentration might affect the hog market price as the number of packing firms declines. Because much of the critical information necessary to construct an accurate model of the industry is not available, we had to make some assumptions. First, it is assumed that pork is a homogenous good, and each packer sets its slaughter (output) believing that rival packers will not change their behavior. The industry consists of identical packing firms. For the model results, the number of packing firms is varied from 1 to 20. Because the United States is both an importer and exporter of pork products with few trade barriers, the model assumes the price of pork is given. Hogs are treated as non-traded, despite the small inflow from Canada. This gives the packers the ability to mark down the price they pay for animals. Although there is evidence of economies to scale in hog slaughter, the extent of these is unknown, and the model assumes no economies of scale. As mentioned, there is also evidence of vertical coordination through contracting and kill capacity constraints. Lacking solid numbers on contracting, these are also ignored in this illustration.

Figure 1 shows how the mark down, or price gap, from the perfectly competitive hog price changes in response to changes in symmetric firm numbers. This mark down represents potential market power of processors to pay less for inputs than would have been the case if both sides were fully competitive. If there are 20 symmetric firms, similar to the situation in the late 1980s, according to this illustration, the price paid to producers for hogs is 95 percent of the perfectly competitive level. As the number of packers falls from 20 to 19 and beyond, the gap on the price paid to suppliers increases. At first the gap remains small. That is, starting from 20 firms, reduced firm numbers do not initially lead to much larger mark downs on the competitive price. When there are 14 firms instead of 20, the hog price is 90 percent of the competitive level instead of 95 percent. As the number of firms falls, the gap increases. Starting from 20 firms, a loss of 6 firms increases the mark down from 5 percent to 10 percent. Going from 14 firms to 8 firms increases the mark down from10 percent to 18 percent. Once firm numbers drop below 5 the mark down or gap increases sharply.

The Herfindahl-Hirschman index indicates that in 1997 the industry consists of 10 symmetric firms, and subsequent observation suggests currently lower values. The illustrative results in Figure 1 show that the range of 8-10 equal sized firms is a critical transition for the magnitudes of the mark downs. Above 10 symmetric firms a change in firm numbers does not cause much change in the mark down. Below 8 symmetric firms, the increases in mark down accelerate. From a public policy perspective it is critical to identify where the industry lies along this relationship. In the case of the model used here, if the industry is presently at 10 firms, policy designed to increase firm numbers may be less critical than policy designed to maintain firm numbers. However, if the industry has the

equivalent of 5 or fewer symmetric firms, like the lamb and beef packing industries, then policy may want to focus on increasing firm numbers.

Figure 1



Missing information is critical

Knowing the precise shape and location of the relationship depicted in Figure 1 is critical to making informed policy choices. The relationship in that figure can only serve as an illustration because critical pieces of the puzzle are missing. To construct the figure, assumptions are made which may incompletely reflect the hog/pork sector. These pieces must be inserted to accurately analyze the consequences of increased packer concentration.

One set of critical information covers the role of vertical integration and coordination. To accurately consider public policy, data on the numbers of hogs contracted and owned as well as the contract terms are required. Such estimates exist, but the quality of this data is suspect. A realistic model would need to divide the market into coordinated and independent hogs. Further, data on costs of packing firms is required because the nature of the cost schedule is critical to the relationship depicted in Figure 1. These include the extent of fixed costs, of economies of scale and of capacity constraints. A particular issue is whether contracting improves the production process and so results in a cost efficiency for vertically coordinated packers.

A major weakness is limited knowledge of the extent of product differentiation and supply-use data by product. Whether packers set quantity or price is critical to the impact of increased concentration. The ability of packers to use their market power hinges on the elasticities of domestic and export demand. These depend on the degree of product

differentiation. We do not have those values and the data to determine them is not currently available. However, with additional data and analysis, it will be possible to narrow the uncertainty of what is occurring in this critical area. Providing that analysis should be a high priority so that public policy can be based on better information.

What Are Some Possible Options?

Background

Both consolidation and increased vertical integration pose a threat to competitive pricing of live animals. We have shown that greater consolidation in the meat packing and processing industry creates a markdown effect on the prices farmers receive for live animals. Likewise, increased captured supplies, via vertical integration and contracting, has the potential to lower prices on average and increase the variability of prices.

Packers are motivated to coordinate their supply of live animals by the large fixed costs associated with a slaughter plant, and the large transactions cost of purchasing thousands of animals on a daily basis. In order to reduce their cost per unit of wholesale meat, packers need to slaughter as many animals as possible. For modern plants, this means thousands of animals each day. The risk of "coming up short" motivates the use of company owned animals and contracted purchases to ensure the appropriate quantity and quality of animals arrive as needed. Transaction costs are reduced by not having to haggle over the price of each load of animals - thus an added attraction to contracting with pre-set prices and quality standards. As the number of providers declines, the packer's transactions costs also decline.

Logically, packers attempt to capture the highest quality animals via contracts and vertical alliances. This can leave the lower quality animals to establish prices in the open market that is not as quality specific. Because payment schemes for most of the packer contracted animals are based on either a spot market price or the Chicago Mercantile Futures price, substantial vertical coordination may create a downward bias in the prices received by most livestock producers.

Offsetting the consolidation and integration effects

Mitigating the downward biases in live animal prices will not be an easy task. The strongest public policy instrument available is anti-trust. Clearly, breaking up the larger packers would help mitigate markdown pricing due to consolidation. However, sound economic rationale, could motivate contracting, vertical integration, and consolidation, so the anti-trust approach might not be justified if monopsony power is only moderate. It is our opinion that alternative public policies do exist that could offset the price impacts of these business structures under moderate monopsony without foregoing their benefits. The focus of these would be on increasing the power of the hog producers. Unfortunately, the livestock producing community has little experience and expertise in using these alternatives and will likely need public policies and assistance to get them functioning.

Cooperation and pooled production and marketing appear to be key to offsetting the impacts of consolidation and integration in today's pork industry. Any strategy that places livestock producers in a more symmetric bargaining position will make it difficult for packers to

exploit prices or contract terms if there is at least a moderate number of packers. It should be more difficult for a packer to terminate a contract without cause (or when more favorable terms can be forced on the producer). Alternatively, the packer in need of animals to fill a daily kill will be compelled to negotiate a more competitive price if producer power is more symmetric. That is, if the amount and quality of animals on the bargaining table is crucial to the full capacity operation of the plant and cannot be replaced easily from another source.

What is critical is the number of hogs that a single supplier (or allied group of suppliers) must control in order to maintain bargaining power with a packer. It appears to be at least 300 thousand to 500 thousand head per year, or approximately the single day double-shift kill for a modern sized slaughter plant each week. This control of numbers also would have to be coincident with a control in quality as well. This is a large number of animals and would require a sizable network (25 to 50 farms) of today's large independent producers. Forming such networks or cooperatives must be nurtured by public policy. Our research at Purdue has demonstrated that there are a variety of ways to structure these entities that may also allow the producers to capture cost reductions and gain access to new (and possibly proprietary) technologies that individual farms would not be capable of obtaining by themselves.

Tax incentives or deductions for members of production and marketing networks, corporations, cooperatives and alliances could provide incentives not only for producers to enter such arrangements, but such policies could also be fashioned to provide disincentives for producers to break away from the group and capture short term gains as a "free rider". Current exemption from anti-trust constraints provides some benefit for cooperative formation. A serious commitment of technical and financial support above that currently available will be needed to develop and encourage new production systems and marketing strategies at the wholesale and retail level to facilitate the building of symmetric power on the part of producers.

The approach needed by these cooperatives and alliances is fundamentally different from traditional livestock marketing cooperatives. In the past, farmers independently produced the animal type of their choice and marketed them on the day of their choice. These marketings were pooled into larger groups and then shipped to a packer. In the cooperative alliances of the future, if they are to be able to increase the bargaining power of producers, the production systems of the cooperating farmers must be coordinated in a way as to provide a steady supply of hogs of uniform quality. The supply chain must be closely managed to deliver animals on a daily basis. Fluctuation in supply is not attractive to a packer and reduces producer leverage. Managing the supply chain in this way will take innovative production practices that may require greater specialization of activities by farm and standardization of mating systems, feeding strategies and genetics.

Marketing orders that set base prices at a particular location with premiums and discounts from that basis for other locals and regulate quality and/or quantity have been popular for several other agricultural commodities. It would be essential for such marketing orders to allow quality premiums to be paid for better quality animals if such a system were adopted for hog production. Otherwise, there would be a disincentive for quality production and the lack of quality hogs would encourage packers to further increase vertical integration and effectively exclude the independent producers from the market.

Finally, any mechanism that ensures that marketing contracts are enforceable, transparent, and "fair" to both sides should be encouraged. This may require legislation that mandates vetting of contracts, bonding of contractors and disclosure of contract terms. Overall, though, caution should be exercised against blanket condemnation of strategies adopted by packers or producers that enable them to compete successfully in an increasingly international marketplace.

Summary and Conclusions

We are witnessing the industrialization of agriculture. The structural changes this involves have been especially pronounced in the pork sector over the last several years. This has involved both integration and concentration which raises important questions about competitiveness of both product and input markets in the pork industry. In addition, there is the issue of who bears risk and who reaps the rewards of the new system as compared with the old one where independent hog producers received returns to management - returns that move up the chain in contracting. Those left outside the new system appear to bear increased risk as independents in the remaining more volatile spot market. They may also be excluded from new technology critical to production and product quality as this becomes increasingly proprietary.

We see evidence of increased concentration to the point where public vigilance is warranted. Concentration indices are high and may be reaching a point where markdown pricing on hogs will be significant and place producers at a clear disadvantage. It is important to have the required information and analysis as soon as possible to properly assess where we are in this respect.

Two major policy options are anti-trust activity on the one hand and increasing the market power of hog producers on the other. In the current free market climate, we cannot realistically expect the breaking up of existing packer concentration. Such actions also can be extremely contentious. However, it may be critically important to prevent further concentration that would greatly increase the markdown of prices paid to producers. Public policy also can assist producers in gaining more market power through highly structured cooperation and tightly pooled production, both of which are foreign to independent hog producers at present.

National Grain and Feed Association

Statement of the
National Grain and Feed Association
Before the
Committee on Agriculture, Nutrition and Forestry
U.S. Senate
February 1, 2000

The National Grain and Feed Association appreciates the opportunity to submit this statement on the Grain Inspection, Packers and Stockyards Administration (GIPSA). Specifically, we will provide comments on the program within GIPSA known as the Federal Grain Inspection Service (FGIS). The FGIS administers the U.S. Grain Standards Act (USGSA) and provides official inspection services to NGFA members. The industry values the credibility and integrity of the official inspection system and believes it provides benefits to U.S. agriculture in domestic and international markets. We note that the number of complaints on the quality of U.S. grades on export shipments by foreign buyers has declined in recent years.

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.

The FGIS has changed in many ways since Congress authorized it in 1976. These changes include a dramatic downsizing of the Agency in the early 1980's and in 1994 a merger with the Packers and Stockyards Administration (PSA) to form the Grain Inspection, Packers and Stockyards Administration. FGIS is largely a service agency to the commercial grain sector. User fees paid by exporters and domestic commercial shippers and receivers fund approximately 75% of Agency operations.

The FGIS and industry maintain a positive working relationship. Agency management routinely meets with NGFA and its Grain Grades and Weights Committee to discuss issues affecting the official system. In 1998, the FGIS announced a strategic plan that, in part, seeks to "increase the efficiency of U.S. grain marketing... to streamline grain inspection and weighing" and "provide ... cost-effective ... grain inspection and weighing services." We are supportive of these goals but remain concerned that FGIS may lack sufficient managerial flexibility to fully achieve them. On the other hand, the Agency has been working with industry to improve automation at export facilities, an effort we applaud.

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The Agency was last re-authorized in 1993 for seven years. Thus, by September 30, 2000, Congress must re-authorize several provisions of the USGSA to allow FGIS to continue providing official services. These provisions include collection of fees for official inspection and weighing activities, the 40% cap on administrative and supervisory costs and the authority for the FGIS Advisory Committee. The 2000 Agency re-authorization provides an opportunity for industry and Congress to consider what changes may be needed in the official inspection system to ensure it can continue to meet the needs of the marketplace.

In this regard, we would like to share our perspective on several issues affecting the official system. Several of these issues are not new having been shared with FGIS management and Congress in the past.

The Operating and Cost Structure of the Domestic and Export Official System Markets

The cost of the official system in domestic and export markets remains a concern to NGFA members.

- Domestic Markets: Official inspection and weighing of U.S. grain in domestic commerce are performed upon request by private agencies granted an exclusive license by FGIS to perform official services in a particular area. In 1993, the GAO study found that the use of the official system in the interior markets has declined because of high costs, inflexible service, consolidation within the industry, and increasing acceptance of unofficial and in-house grades by the market. While it appears that utilization of the domestic official system may have stabilized somewhat in recent years, a 1999 survey of NGFA members indicates that cost of service remains a strong concern.

  As a result of the GAO survey, the NGFA recommended during the 1993 re-authorization of the Agency that Congress require FGIS to conduct pilot programs to open selected interior official territories to competitive bidding for services. The Agency began a series of pilot programs in 1995 and the results indicate that granting FGIS permanent authority to allow increased competition within the domestic official system may be beneficial.

- Export Markets: The U.S. Grain Standards Act (USGSA) requires that export grain be officially inspected and weighed by FGIS personnel. Over the past 10 years, the FGIS has experienced significant financial losses, seriously depleting the Agency's financial reserves. As a result, the FGIS has instituted a series of fee increases over the last several years that has resulted in making the cost of official inspection one of the top operating expenses at export elevators. While the Agency reported approximately $1.8 million in profits at the end of Fiscal Year 1999, the cost of official inspections at export locations and future management of those costs remains a concern. We believe

managerial that both FGIS and industry would benefit if FGIS management had additional flexibility to control costs and maximize operating efficiency.

On February 2, 2000, the NGFA's Grain Grades and Weights Committee will meet to discuss a number of policy options to assist FGIS efforts in fulfilling its role under the USGSA. One option under serious consideration by NGFA would shift FGIS from a more traditional government agency model to a Performance Based Organization (PBO) within government. The PBO concept was designed as a business model for government agencies heavily focused on service to the private sector, a description that fits much of FGIS operations as well. The PBO concept has been used successfully in the federal government's Student Financial Aid.

While several questions remain, we believe the PBO concept is attractive because it may offer FGIS greater flexibility in the way its manages its operations while retaining strong federal government oversight of the inspection functions. To move forward with this concept would require authorizing legislation. NGFA's committee will be studying the pros and cons of this concept and decide whether to make a formal legislative proposal shortly.

Another policy option that should be considered is reducing 40% cap on administrative and supervisory fees to 20%. Reducing the 40% cap would be consistent with trends within private industry. Furthermore, the Agency reported in 1995 that administrative and supervisory costs represented 23% of total program costs. Thus, a reduction to 20% may also be consistent with trends within the Agency itself.

FGIS Advisory Committee

The FGIS Advisory Committee was created to provide advice to the FGIS Administrator on implementation of the USGSA. Over the years, the direct users of the official inspection system – those actually paying for the service – have increasingly come to question the relevancy of the FGIS Advisory Committee to assisting the Agency in its responsibilities. We think a stronger representation by direct users on the Advisory Committee would help address this situation and recommend that Congress authorize that that at least 10 of the 15 advisory committee members represent companies that are direct users of the official system.

Biotechnology

The introduction of corn and soybeans enhanced through the techniques of modern biotechnology for increased insect resistance and herbicide tolerance has raised concerns in some foreign markets and creates the need for accurate and affordable tests to quickly distinguish these new varieties from those developed through conventional plant breeding. Responding to a recommendation from NGFA, the FGIS has announced its plan to establish a reference laboratory at its Technical Center in Kansas City, Missouri to verify the accuracy and repeatability of test kits used to detect biotechnology-enhanced crops. We support this approach.

The FGIS has also indicated that it is considering developing standards for the identity preservation (IP) of grains that either possess or do not possess traits introduced through the techniques of modern biotechnology. The procedures concerning the process to ensure the delivery of non-biotechnology-enhanced commodities often vary between customers. Therefore, we believe that they should be left, whenever possible, to contractual agreements between buyer and seller at this time.

Reauthorization

As noted previously, the FGIS was re-authorized in 1993 until September 30, 2000, i.e., for a seven year time frame. We understand that FGIS is suggesting that it be re-authorized for 10 years. We believe that in today's rapidly changing global business environment a 10-year reauthorization is simply too long. In fact, we believe that rather than extending the re-authorization period from seven to ten years, Congress should consider reducing the period of reauthorization to no more than five years.

Conclusion

Through its efforts to maintain accuracy and consistency in the official inspection and weighing system, the FGIS assists in maintaining the economic efficiency of the U.S. grain marketing system. The credibility and integrity of the official system is very important to grain handlers and very beneficial to U.S. exporters. However, managing system costs and improving FGIS management capabilities to reorganize to enhance efficiency and productivity of FGIS employees present challenges to the long-term viability of the system. The upcoming re-authorization debate presents an opportunity for Congress to consider potential changes to the official system to ensure that it will continue to provide a needed and cost-effective market service.