

Dated: December 12, 2016.

**Bruce Summers,**

*Associate Administrator, Agricultural Marketing Service.*

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## DEPARTMENT OF AGRICULTURE

### Grain Inspection, Packers and Stockyards Administration

#### 9 CFR Part 201

RIN 0580-AB25

#### Scope of Sections 202(a) and (b) of the Packers and Stockyards Act

**AGENCY:** Grain Inspection, Packers and Stockyards Administration, USDA.

**ACTION:** Interim final rule; request for comments.

**SUMMARY:** The Department of Agriculture's (USDA) Grain Inspection, Packers and Stockyards Administration (GIPSA), Packers and Stockyards Program (P&SP) is amending the regulations issued under the Packers and Stockyards Act, 1921, as amended and supplemented (P&S Act). GIPSA is adding a paragraph addressing the scope of sections 202(a) and (b) of the P&S Act. This interim final rule clarifies that conduct or action may violate sections 202(a) and (b) of the P&S Act without adversely affecting, or having a likelihood of adversely affecting, competition. This interim final rule reiterates USDA's longstanding interpretation that not all violations of the P&S Act require a showing of harm or likely harm to competition. The regulations would specifically provide that the scope of section 202(a) and (b) encompasses conduct or action that, depending on their nature and the circumstances, can be found to violate the P&S Act without a finding of harm or likely harm to competition. This interim final rule finalizes a proposed amendment that GIPSA published on June 22, 2010. GIPSA is now publishing as an interim final rule what was proposed on June 22, 2010, with slight modifications, in order to allow additional comment on these provisions.

**DATES:** This interim final rule is February 21, 2017. Interested persons are invited to submit written comments on this interim final rule on or before February 21, 2017.

**ADDRESSES:** We invite you to submit comments on this interim final rule. You may submit comments by any of the following methods:

- *Mail:* M. Irene Omade, GIPSA, USDA, 1400 Independence Avenue SW., Room 2542A-S, Washington, DC 20250-3613.
  - *Hand Delivery or Courier:* M. Irene Omade, GIPSA, USDA, 1400 Independence Avenue SW., Room 2530-S, Washington, DC 20250-3613.
  - *Internet:* <http://www.regulations.gov>. Follow the on-line instructions for submitting comments.
- Instructions:* All comments should make reference to the date and page number of this issue of the **Federal Register**. All comments received will be included in the public docket without change, including any personal information provided. Regulatory analyses and other documents relating to this rulemaking will be available for public inspection in Room 2542A-S, 1400 Independence Avenue SW., Washington, DC 20250-3613 during regular business hours. All comments will be available for public inspection in the above office during regular business hours (7 CFR 1.27(b)). Please call the Management and Budget Services staff of GIPSA at (202) 720-8479 to arrange a public inspection of comments or other documents related to this rulemaking.

**FOR FURTHER INFORMATION CONTACT:** S. Brett Offutt, Director, Litigation and Economic Analysis Division, P&SP, GIPSA, 1400 Independence Ave, SW., Washington, DC 20250, (202) 720-7051, [s.brett.offutt@usda.gov](mailto:s.brett.offutt@usda.gov).

**SUPPLEMENTARY INFORMATION:** The first section that follows provides background and a summary of the regulatory text for § 201.3(a) and (b) in this interim final rule as compared to the regulatory wording for § 201.3(c) and (d) in the 2010 proposed rule. The second section provides background information about this rule. The third section provides a summary of the public comments received on the proposed rule and at the relevant USDA/Department of Justice Joint Competition Workshops that occurred during the comment period. The fourth section discusses the proposal of new §§ 201.210, 201.211, and 201.214, in this issue of the **Federal Register**. The last section provides the required impact analyses including the Regulatory Flexibility Act, the Paperwork Reduction Act, Civil Rights Analysis, and the relevant Executive Orders.

#### I. Summary of Changes From the 2010 Proposed Rule

##### *Section 201.3 as Proposed in June 2010*

In the proposed rule published in the **Federal Register** on June 22, 2010 [75

FR 35338], GIPSA proposed a new § 201.3, "Applicability of regulations in this part," providing four (4) subsections to describe, in certain respects, the application of the regulations in 9 CFR part 201. These subsections were designated § 201.3(a) through § 201.3(d). Subsection 201.3(c) described the appropriate application of sections 202(a) and (b) of the P&S Act (7 U.S.C. 192(a) and (b)).

In this current rule, GIPSA is re-designating the existing undesignated paragraph in § 201.3 as § 201.3(b), and is adding back the subject heading, "Effective dates" to this paragraph.

GIPSA is amending § 201.3 with the addition of proposed § 201.3(c), with slight modifications. Because this provision is of primary importance, GIPSA is designating it as the first of two paragraphs in § 201.3 and changing its designation from (c) to (a). GIPSA has made slight modifications including a grammatical edit and also modified a few words to make the language internally consistent and also consistent with the language in new proposed §§ 201.210, 201.211, and 201.214, published concurrently in this issue of the **Federal Register** as separate proposed rules.

## II. Background

### A. Development of the Rule

Prior to issuing the initial proposed regulations in 2010, GIPSA held three public meetings in October 2008, in Arkansas, Iowa, and Georgia to gather comments, information, and recommendations from interested parties. Attendees at these meetings were asked to give input on the elements of the 2008 Farm Bill and other issues of concern under the P&S Act. In 2010, USDA and the Department of Justice held five joint public workshops to explore competition issues affecting agricultural industries in the 21st century and the appropriate role for antitrust and regulatory enforcement in those industries. These workshops were held in Ankeny, Iowa (Issues of Concern to Farmers, March 12, 2010); Normal, Alabama (Poultry Industry, May 21, 2010); Madison, Wisconsin (Dairy Industry, June 25, 2010); Fort Collins, Colorado (Livestock Industry, August 27, 2010); and Washington, District of Columbia (Margins, December 8, 2010). The Secretary informed attendees of the workshop in Fort Collins, Colorado that their comments provided that day would be considered in the development of this rulemaking. The Fort Collins workshop addressed issues in the cattle, hog, and other animal

sectors. Attendees provided comments on concentration in livestock markets, buyer power, and enforcement of the P&S Act. GIPSA incorporated relevant comments from the Madison, Wisconsin and Fort Collins, Colorado workshops into the text of the wording of the final rule published on December 9, 2011.

The regulations in this current interim final rule also reflect comments, information, and recommendations received in all those meetings.

On June 22, 2010, GIPSA published the proposed rule [75 FR 35338] upon which this interim final rule is based. The background information presented in the proposed rule remains pertinent to this interim final rule. Some of this background information is presented again here.

In that proposed rule, GIPSA proposed a multi-faceted rule and sought public input. During a 5-month comment period, GIPSA received over 61,000 comments from a wide variety of stakeholders. Some commenters addressed issues associated with this interim final rule. GIPSA published a final rule in 2011 that included modifications to address concerns expressed by commenters. The final rule addressed most, but not all, of the requirements of the Food, Conservation, and Energy Act of 2008 (Pub. L. 110–246) (2008 Farm Bill); however, for the reasons described in further detail below, GIPSA never implemented a final § 201.3(c) following the 2010 public notice and comment period. The 2010 proposed rule also proposed three other regulations, §§ 201.210, 201.211, and 201.214, that GIPSA has restructured and rewritten and is publishing as two separate proposed rules concurrent with this rule.

Proposed § 201.210, “Unfair, unjustly discriminatory and deceptive practices or devices by packers, swine contractors, or live poultry dealers,” and § 201.211, “Undue or unreasonable preferences or advantages” further clarify and define the provisions of § 201.3(a). Proposed § 201.214, “Poultry Grower Ranking Systems” provides criteria which would be used in considering whether a live poultry dealer has used a poultry grower ranking system in an unfair, unjustly discriminatory, or deceptive manner or in a way that gives an undue or unreasonable preference or advantage to any poultry grower or subjects any poultry grower to an undue or unreasonable prejudice or disadvantage.

Beginning with the fiscal year (FY) 2012 appropriations act, USDA was precluded from finalizing some of the regulations as proposed in June 2010. Section 201.3(c), “Scope of Sections

202(a) and (b) of the Act,” §§ 201.210, 201.211, and 201.214, published as part of the June 22, 2010, proposed rule, were included in the restrictions in the appropriations acts. Until FY 2016, appropriations acts continued to preclude the finalization of §§ 201.3(c), 201.210, 201.211, and 201.214.

Section 201.3(a), “Applicability to live poultry dealers,” and § 201.3(d), “Effective dates,” proposed in June 2010, were published on December 9, 2011 [76 FR 76874], as a final rule with some changes. At that time, the designation of proposed paragraph (d) was changed to (b).

Section 731, Division A, of the Consolidated and Further Continuing Appropriations Act, 2015 (Pub. L. 113–235), required the Secretary to rescind what was then § 201.3(a), “Applicability to live poultry dealers,” leaving paragraph (b) as the only paragraph in § 201.3. As a result, GIPSA removed the designation for this paragraph as paragraph (b) and also removed its subject heading, “Effective dates.” This was accomplished by a final rule published on February 5, 2015 [80 FR 6430].

Neither the FY 2016 appropriations act nor the FY 2017 continuing appropriations act precludes GIPSA from publishing §§ 201.3(c), 201.210, 201.211, or 201.214 as final rules.

#### B. Purpose of the Regulatory Action

Section 202 of the P&S Act provides that “[i]t shall be unlawful for any packer or swine contractor 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 engage in certain prohibited conduct. Section 202(a) prohibits “any unfair, unjustly discriminatory, or deceptive practice or device.” Section 202(b) prohibits “any undue or unreasonable preference or advantage” or “any undue or unreasonable prejudice or disadvantage.” USDA has consistently taken the position that, in some cases, a violation of section 202(a) or (b) can be proven without proof of predatory intent, competitive injury, or likelihood of competitive injury.<sup>1</sup> At the same time, USDA has always understood that an act or practice’s effect on competition can be relevant<sup>2</sup> and, in certain circumstances, even

<sup>1</sup> *In re Ozark County Cattle Co.*, 49 Agric. Dec. 336, 365 (1990); 1 John H. Davidson et al., *Agricultural Law* section 3.47, at 244 (1981).

<sup>2</sup> *See, In re Sterling Colo. Beef Co.*, 39 Agric. Dec. 184, 235 (1980) (considering and rejecting respondent packer’s business justification for challenged conduct).

dispositive<sup>3</sup> with respect to whether that act or practice violates sections 202(a) and/or (b).

As we explained in the proposed rule, the longstanding agency position that, in some cases, a violation of section 202(a) or (b) can be proven without proof of likelihood of competitive injury is consistent with the language and structure of the P&S Act, as well as its legislative history and purposes. Neither section 202(a) nor section 202(b) contains any language limiting the application of those sections to acts or practices that have an adverse effect on competition, such as acts “restraining commerce.” Instead, these provisions use terms including “deceptive,” “unfair,” “unjust,” “undue,” and “unreasonable”—which are commonly understood to encompass more than anticompetitive conduct.<sup>4</sup> This is in direct contrast to subsections (c), (d), and (e), which expressly prohibit only those acts that have the effect of “restraining commerce,” “creating a monopoly,” or producing another type of antitrust injury. The fact that Congress expressly included these limitations in subsections (c), (d), and (e), but not in subsections (a) and (b), is a strong indication that Congress did not intend subsections (a) and (b) to be limited to instances in which there was harm to competition. And Congress confirmed the agency’s position by amending the P&S Act to specify specific instances of conduct prohibited as unfair that do not involve any inherent likelihood of competitive injury.<sup>5</sup>

USDA’s interpretation of sections 202(a) and (b) is also consistent with the interpretation of other sections of the P&S Act using similar language—sections 307 and 312 (7 U.S.C. 208 and 213). Courts have recognized that the proper analysis under these provisions

<sup>3</sup> *See, Armour & Co. v. United States*, 402 F.2d 712, 717 (7th Cir. 1968) (a coupon promotion plan (here coupons for fifty cents off specified packages of bacon) is not per se unfair and violates section 202(a) if it is implemented with some predatory intent or carries some likelihood of competitive injury); *In re IBP, Inc.*, 57 Agric. Dec. 1353, 1356 (1998) (contractual right of first refusal at issue violated section 202 “because it has the effect or potential of reducing competition”).

<sup>4</sup> When the P&S Act was enacted, *Webster’s New International Dictionary* defined “deceptive” as “[t]ending to deceive; having power to mislead, or impress with false opinions”; “unfair” as “[n]ot fair in act or character; disingenuous; using or involving trick or artifice; dishonest; unjust; inequitable” (2d. definition); and “unjust” as “[c]haracterized by injustice; contrary to justice and right; wrongful.” *Webster’s New International Dictionary* 578, 2237, 2238, 2245, 2248 (1st ed. 1917). This is the same understanding of the terms today.

<sup>5</sup> *See* sections 409(c) and 410(b).

depends on “the facts of each case,”<sup>6</sup> and that these sections may apply in the absence of harm to competition or competitors.<sup>7</sup>

The legislative history and purposes of the P&S Act also support USDA’s position. The P&S Act “is a most comprehensive measure and extends farther than any previous law in the regulation of private business, in time of peace, except possibly the interstate commerce act.”<sup>8</sup> In amending the P&S Act, Congress made clear that its goals for the statute extended beyond the protection of competition. In 1935, for instance, when Congress first subjected live poultry dealers to sections 202(a) and (b), Congress explained in the statute itself that “[t]he handling of the great volume of live poultry . . . is attendant with various unfair, deceptive, and fraudulent practices and devices, resulting in the producers sustaining sundry losses and receiving prices far below the reasonable value of their live poultry. . . .”<sup>9</sup> Similarly, the House Committee Report regarding the 1958 amendments stated that “[t]he primary purpose of [the P&S Act] is to assure fair competition and fair trade practices” and “to safeguard farmers . . . against receiving less than the true market value of their livestock.”<sup>10</sup> The Report further observed that protection extends to “unfair, deceptive, unjustly discriminatory” practices by “small” companies in addition to “monopolistic practices.”<sup>11</sup> In accordance with this legislative history, courts and commentators have recognized that the purposes of the P&S Act are not limited to protecting competition.<sup>12</sup>

Four courts of appeals have disagreed with USDA’s interpretation of the P&S

Act and have concluded (in cases to which the United States was not a party) that plaintiffs could not prove their claims under sections 202(a) and/or (b) without proving harm to competition or likely harm to competition.<sup>13</sup> After carefully considering the analyses in these opinions, USDA continues to believe that its longstanding interpretation of the P&S Act is correct. These court of appeals opinions (two of which were issued over vigorous dissents)<sup>14</sup> are inconsistent with the plain language of the statute; they incorrectly assume that harm to competition was the only evil Congress sought to prevent by enacting the P&S Act; and they fail to defer to the Secretary of Agriculture’s longstanding and consistent interpretation of a statute administered by the Secretary. To the extent that these courts failed to defer to USDA’s interpretation of the statute because that interpretation had not previously been enshrined in a regulation,<sup>15</sup> this new regulation may constitute a material change in circumstances that warrants judicial reexamination of the issue.<sup>16</sup>

Although it is not necessary in every case to demonstrate competitive injury in order to show a violation of sections 202(a) and/or (b), any act that harms competition or is likely to harm competition may violate the statute. How a competitive injury or the likelihood of a competitive injury manifests itself depends critically on whether the target of the act or practice is a competitor (e.g., a packer harms other packers), or whether the target of the act or practice operates at a different level of the livestock or poultry production process (e.g., a packer harms a livestock producer). Competitive injury or the likelihood of competitive injury may occur when an act or practice improperly forecloses competition in a large share of the

market through exclusive dealing, restrains competition among packers, live poultry dealers or swine contractors or otherwise represents a use of market power to distort competition.<sup>17</sup> Competitive injury or the likelihood of competitive injury also may occur when a packer, swine contractor, or live poultry dealer wrongfully depresses prices paid to a livestock producer, swine production contract grower, or poultry grower below market value or impairs the livestock producer, swine production contract grower, or poultry grower’s ability to compete with other producers or growers.

To establish an actual or likely competitive injury, it is not necessary to show that a challenged act or practice had a likely effect on resale price levels. Even the antitrust laws do not require such a showing. The P&S Act is broader than the antitrust laws and, therefore, such a requirement of showing effect on resale price levels is not necessary to establish competitive injury under section 202 of the P&S Act (though such a showing would suffice).

### III. Discussion of Comments

The proposed rule published on June 22, 2010, (75 FR 35338) provided a 60-day comment period to end on August 23, 2010. In response to requests for an extension of time to file comments, on July 28, 2010, GIPSA extended the comment period to end on November 22, 2010 (75 FR 44163). Commenters covered the spectrum of those affected by the rule, including livestock producers and poultry growers, packers and live poultry dealers, trade associations representing both production and processing, plant workers, and consumers. GIPSA considered all comments postmarked or electronically submitted by November 22, 2010. GIPSA received over 61,000 comments, which addressed the rule generally as well as specific provisions. GIPSA considered written comments as well as comments received at two public meetings, on June 25, 2010, and August 27, 2010, conducted jointly by USDA and the Department of Justice. Because these “Workshops on Competition in Agriculture” were held during the comment period for the proposed rule, the Secretary announced that any comments made in those forums would be considered comments on the proposed rule.

Comments on proposed § 201.3(c) were sharply divided with respect to

<sup>6</sup> *Capitol Packing Co. v. United States*, 350 F.2d 67, 76 (10th Cir. 1965); see also, *Spencer Livestock Comm’n Co. v. USDA*, 841 F.2d 1451, 1454 (9th Cir. 1988).

<sup>7</sup> See, e.g., *Spencer*, 841 F.2d at 1455 (Section 312 covers “a deceptive practice, whether or not it harmed consumers or competitors.”).

<sup>8</sup> H.R. Rep. 67–77, at 2 (1921); see also, *Swift & Co. v. United States*, 308 F.2d 849, 853 (7th Cir. 1962) (“The legislative history showed Congress understood the sections of the [P&S Act] under consideration were broader in scope than antecedent legislation such as the Sherman Antitrust Act, sec. 2 of the Clayton Act, 15 U.S.C. 13, sec. 5 of the Federal Trade Commission Act, 15 U.S.C. 45 and sec. 3 of the Interstate Commerce Act, 49 U.S.C. 3.”).

<sup>9</sup> Public Law 74–272, 49 Stat. 648, 648 (1935).

<sup>10</sup> H.R. Rep. No. 85–1048 (1957), reprinted in 1958 U.S.C.C.A.N. 5212, 5213 (emphasis added).

<sup>11</sup> *Id.* at 5213.

<sup>12</sup> See, e.g., *Stafford v. Wallace*, 258 U.S. 495, 513–14 (1922); *Spencer*, 841 F.2d at 1455; *United States v. Perdue Farms, Inc.*, 680 F.2d 277, 280 (2d Cir. 1982); *Bruhn’s Freezer Meats of Chicago, Inc. v. USDA*, 438 F.2d 1332, 1336 (8th Cir. 1971); *Bowman v. USDA*, 363 F.2d 81, 85 (5th Cir. 1966); *United States v. Donahue Bros.*, 59 F.2d 1019, 1023 (8th Cir. 1932).

<sup>13</sup> *Terry v. Tyson Farms, Inc.* 604 F.3d 272, 280 (6th Cir. 2010) (“[I]n order to succeed on a claim under §§ 192(a) and (b) of the [P&S Act], a plaintiff must show an adverse effect on competition.”); *Wheeler v. Pilgrim’s Pride Corp.*, 591 F.3d 355, 363 (5th Cir. 2009) (*en banc*) (“To support a claim that a practice violates subsection (a) or (b) of § 192 [of the P&S Act] there must be proof of injury, or likelihood of injury, to competition.”); *Been v. O.K. Indus., Inc.*, 495 F.3d 1217, 1238 (10th Cir. 2007) (An “unfair practice” under section 202(a) of the P&S Act is one that injures or is likely to injure competition); *London v. Fieldale Farms Corp.*, 410 F.3d 1295, 1303 (11th Cir. 2005) (P&S Act prohibits only those unfair, discriminatory, or deceptive practices that adversely affect or are likely to adversely affect competition).

<sup>14</sup> *Wheeler*, 591 F.3d at 371–85 (Garza, J., dissenting); *Been*, 495 F.3d at 1238–43 (Hartz, J., concurring in part and dissenting in part).

<sup>15</sup> See *Been*, 495 F.3d at 1226–27.

<sup>16</sup> See *Nat’l Cable & Telecomm. Ass’n v. Brand X Internet Servs.*, 545 U.S. 967, 982–84 (2005).

<sup>17</sup> See, e.g., Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals’ Costs to Achieve Power over Price*, 96 Yale L.J. 209 (1986); 11 Philip E. Areeda & Herbert Hovenkamp, *Antitrust Law* 1821 (2d ed. 2005).

harm to competition. Those supporting the proposal pointed out it would provide legal relief for farmers and ranchers who suffer because of unfair actions, such as false weighing and retaliatory behavior, without having to show competitive harm to the industry. Opposing comments relied heavily on the fact that several of the United States Courts of Appeals have ruled that harm to competition (or the likelihood of harm to competition) is a required element to find a violation of sections 202(a) and (b) of the P&S Act.

Those supporting proposed § 201.3(c) included numerous livestock producers and poultry growers and organizations representing the interests of farmers and ranchers. Commenters supporting proposed § 201.3(c) pointed out that it would reduce the costs of litigation for poultry growers and livestock producers who suffer because of unfair actions, such as false weighing and retaliation. Proposed § 201.3(c), according to some commenters, corrects the analytical framework of the P&S Act and ensures that the courts grant a higher level of deference to USDA's interpretation of the P&S Act. They believed it was wrong to require a demonstration of harm to competition to the whole industry stemming from an unfair practice targeting an individual grower or producer in order to violate section 202(a) of the P&S Act, and that proposed § 201.3(c) would remove an undue barrier to relief.

Commenters in favor of proposed § 201.3(c) further pointed out the imbalance in power between livestock producers and packers and noted that without this provision, the packers are inoculated against recourse by a livestock producer because the livestock producer is small and overmatched relative to the much larger and more well-resourced packer. A common theme among supporters was that proposed § 201.3(c) allowed farmers and ranchers to seek redress by showing that they were individually harmed in cases such as false weighing or retaliatory behavior, rather than requiring a showing of harm to competition in the industry. Commenters felt that the packers and poultry companies were given a free pass to act unfairly toward livestock producers, swine production contract growers, and poultry growers knowing that proving harm to competition to the industry would be difficult, if not impossible, in many situations.

Many of the supporting comments also addressed the plain language and intent of section 202 of the P&S Act and opined that the recent court decisions were based on incorrect interpretations

of the law. Commenters wrote that proposed § 201.3(c) correctly interpreted the plain language of section 202 and the legislative history of the P&S Act.

Commenters opposing proposed § 201.3(c) included many meat packers, live poultry dealers, and organizations representing packers and poultry companies. The opposing comments stated that the P&S Act had always been considered an antitrust statute and therefore, GIPSA should be required to show competitive harm to allege a violation of section 202(a). They also expressed concern that a flood of litigation would ensue if the scope of section 202(a) did not remain closely aligned with case law. Commenters opposed to the rulemaking asserted that allowing allegations of section 202(a) violations without a showing of harm or likely harm to competition would enable swine production contract growers, poultry growers, or livestock producers to sue a swine contractor, live poultry dealer, or packer for a broad range of adverse circumstances affecting them. The comments went on to say that this would guarantee swine production contract growers, poultry growers, and livestock producers a profit on every transaction, a standard afforded in no other industry. In turn, this would reduce the number of swine production contract growers, poultry growers, and livestock producers with whom companies would do business.

Opposing comments relied heavily on the fact that several United States Courts of Appeals have ruled that harm to competition (or the likelihood of harm to competition) is a required element to find a violation of sections 202(a) and (b) of the P&S Act. These commenters stated that because of the decisions in these circuit courts, GIPSA lacked authority to implement proposed § 201.3(c). Several large packers and poultry companies wrote that the proposed § 201.3(c), if implemented, would be in direct conflict with circuit court decisions in the geographic regions in which they do business. One packer commented that livestock producers would bear the cost of determining the legality of an expanded scope of sections 202(a) and 202(b).

Many opposing commenters felt that proposed § 201.3(c) would lead to a large increase in frivolous litigation and greatly increase operational costs for packers and poultry companies. Commenters felt that an increase in frivolous litigation would lead to a decrease in the use of the value-based pricing. Commenters opposed allowing livestock producers to file lawsuits based on their thoughts of what is unfair. Some commenters believed that

proposed § 201.3(c) would eliminate the requirement to show any harm at all. A common concern presented by those in opposition to the proposed change to § 201.3 was that while section 202(a) prohibits unfair, unjustly discriminatory, or deceptive practices, the P&S Act does not define what types of conduct would be classified as such. Of particular concern to these commenters was the prospect that GIPSA may bring actions under section 202(a) without a finding of harm to competition which would encourage livestock producers to sue firms subject to the P&S Act for any conduct having an adverse effect on livestock producer interests. While most of the comments focused on unfair conduct that could violate section 202(a), a few comments mentioned section 202(b) as well. These comments set forth concerns calling for regulatory guidance as to what conduct GIPSA would deem as unfair, unjustly discriminatory, or deceptive, and an undue preference or advantage in violation of the P&S Act, especially when there was no showing of harm to competition.

*Agency response:* GIPSA did not make the specific changes to proposed § 201.3(c) requested by comments. However, GIPSA is proposing new rule language in proposed rules §§ 201.210, 201.211, and 201.214, that provide the guidance commenters were seeking. GIPSA also modified a few words in § 201.3(c) to make the language internally consistent and to make it consistent with the language in new proposed §§ 201.210, 201.211, and 201.214, published concurrently in this issue of the **Federal Register** as two separate proposed rules. Specifically, proposed §§ 201.210 and 201.211 discuss “conduct or action” and GIPSA has modified the references to “conduct” in proposed § 201.3(c) to “conduct or action.” GIPSA also changed the reference to “challenged act or practice” to “challenged conduct or action,” again for consistency with proposed §§ 201.210 and 201.211 and to make the language in § 201.3(a) internally consistent. In the proposed rule for § 201.214 in this issue of the **Federal Register**, GIPSA proposes listing the failure to use a poultry grower ranking system in a fair manner after applying the criteria in § 201.214 as a tenth type of “challenged conduct or action” under § 201.210(b). GIPSA also made a minor grammatical edit and changed all references to “section” to “sections.” GIPSA believes the paragraph proposed on June 22, 2010, as § 201.3(c) (“Scope of Sections 202(a) and (b) of the Act.”) is of primary

importance. As a result, the paragraph is designated as paragraph (a) and the current text in § 201.3 is designated as paragraph (b).

It is the longstanding position of the Secretary of Agriculture that a violation of section 202(a) or (b) can be proven without evidence of competitive injury or the likelihood of competitive injury. The Secretary's position is consistent with the language and structure of the P&S Act, as well as its legislative history and purposes. Sections 202(c), 202(d), and 202(e) of the P&S Act include "restraint" and "monopoly" language, some of which resembles language in the Clayton Act, 15 U.S.C. 12–27. Neither section 202(a) nor section 202(b) contains language limiting the application to conduct or action that has an adverse effect, or the likelihood of an adverse effect, on competition, such as acts "restraining commerce." Sections 202(a) and 202(b) are tort-like provisions that are concerned with unfair practices, discrimination, and preferential treatment, but not with restraint of trade or monopolistic activities.

Analysis of the Federal Trade Commission Act, 15 U.S.C. 41–58, as amended, (FTC Act) is helpful in illustrating the Secretary's position on the scope of sections 202(a) and 202(b) of the P&S Act. Congress considered the FTC Act in drafting the P&S Act as it incorporated portions of the FTC Act by reference into the P&S Act. Section 5 of the FTC Act, now codified at 15 U.S.C. 45, states, "[u]nfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful." Thus, in the FTC Act, Congress makes a distinction between "unfair methods of competition" and "unfair or deceptive acts or practices." In drafting the P&S Act, Congress chose to prohibit any "unfair, unjustly discriminatory, or deceptive practice or device," and the making or giving of "any undue or unreasonable preference or advantage . . ." without limiting the unfair practices or devices, discrimination, or preferential treatment to only those involving competition. The Supreme Court of the United States has examined the scope of Section 5 of the FTC Act, noting that unfair practices are not limited to those likely to have anticompetitive consequences after the manner of the antitrust laws, nor are unfair practices in commerce confined to purely competitive behavior.<sup>18</sup> The FTC Act's phrase, "'unfair or deceptive

acts or practices'" makes the consumer, who may be injured by an unfair trade practice, of equal concern, before the law, with the merchant or manufacturer injured by the unfair methods of a dishonest competitor."<sup>19</sup> The Court also noted, upon consideration of legislative and judicial authorities, that the Federal Trade Commission considers public values beyond simply those enshrined in the letter or encompassed in the spirit of the antitrust laws.<sup>20</sup>

Recent circuit court decisions have found that a showing of competitive harm, or a likelihood of competitive harm, is required to substantiate a violation of sections 202(a) and 202(b) of the P&S Act. In one of these cases, *Wheeler v. Pilgrim's Pride Corp.*,<sup>21</sup> while the majority opinion required a finding of harm to competition, the dissenting opinion agreed with the district court's ruling that sections (a) and (b) of 202 do not contain language limiting their application to actions which have an adverse effect on competition.<sup>22</sup> The court in another case, *Been v. O.K. Indus., Inc.*,<sup>23</sup> declined to defer to USDA's interpretation of "unfair" practices under section 202(a) of the P&S Act, in part, because "the Secretary has not promulgated a regulation applicable to the practices the Growers allege violate § 202(a)." <sup>24</sup> The court, however, stated that "[r]egulations promulgated by an agency exercising its congressionally granted rule-making authority" are entitled to deference,<sup>25</sup> implying that such regulation, once enacted by USDA, would be entitled to deference. Therefore, while decisions of the courts of appeals support comments in opposition to amending § 201.3, these same decisions have also pointed to a need for the very rulemaking the addition of paragraph (a) to § 201.3 provides.

An initial increase in litigation costs is a likely result of this rule, as the industry and the courts are setting precedents for the interpretation of § 201.3. However, the litigation costs and the number of lawsuits are expected to decrease after precedent setting decisions are established. In order to place some parameters on conduct or action that constitutes unfair, unjustly discriminatory, and deceptive practices or devices under section 202(a), and on conduct or action that constitutes undue

or unreasonable preferences or advantages under section 202(b), and to address concerns raised by commenters about what those terms mean, GIPSA is publishing concurrently with this interim final rule, proposed rules that will include revised §§ 201.210, 201.211, and 201.214, which will help clarify the conduct or action GIPSA considers violations of sections 202(a) and 202(b) of the P&S Act.

Contrary to some comments, § 201.3(a) does not stand for the proposition that GIPSA never has to demonstrate that the challenged conduct or action adversely affects competition. Instead, § 201.3(a) solely reiterates GIPSA's longstanding position that a finding that the challenged conduct or action adversely affects or is likely to adversely affect competition is not necessary in all cases. Certain conduct is prohibited because it is unfair, unjustly discriminatory or deceptive even though there may be no harm, or likelihood of harm, to competition. Likewise, certain conduct is prohibited because it creates an unfair preference or advantage even though there may be no harm, or likelihood of harm, to competition. This rule, combined with the specific examples of prohibited conduct in proposed § 201.210 and the criteria the Secretary will consider as set forth in proposed § 201.211, will assist industry participants in understanding which behaviors violate sections 202(a) and 202(b) of the P&S Act.

#### IV. Interim Final Rule and Request for Comments

As previously discussed, GIPSA published a notice of proposed rulemaking in June, 2010, that, *inter alia*, proposed regulatory text relating to the scope of the P&S Act. GIPSA solicited comments over a 5 month period and received thousands of comments on this aspect of the proposed rule. Accordingly, the agency has fulfilled the notice and comment requirements of the Administrative Procedure Act. However, given the significant level of stakeholder interest in this regulatory provision, the intervening six years, and in the interests of open and transparent government, the agency has decided to promulgate the rule as an interim final rule and provide an additional opportunity for public comment. The agency will consider all comments received by the date indicated in the **DATES** section of this interim final rule with request for comments. After the comment period closes, the agency intends to publish another document in the **Federal Register**. The document will

<sup>18</sup> *Id.*, at 244. (quoting H.R.Rep.No.1613, 75th Cong., 1st Sess., 3 (1937).

<sup>20</sup> *Id.*, at 244.

<sup>21</sup> 591 F. 3d 355 (5th Cir. 2009).

<sup>22</sup> *Id.* at 377 (Garza, J., dissenting).

<sup>23</sup> 495 F. 3d 1217 (10th Cir. 2007).

<sup>24</sup> *Id.* at 1226–27.

<sup>25</sup> *Id.* at 1226.

<sup>18</sup> *FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233 (1972).

include a discussion of any comments received and whether any amendments will be made to the rule.

#### V. Concurrent Publication of Proposed §§ 201.210, 201.211, and 201.214

While some appellate courts have determined that a showing of competitive injury, or likelihood of competitive injury, is required to allege a violation of sections 202(a) or 202(b), some dissenting opinions agreed with USDA's interpretation of sections 202(a) and 202(b)<sup>26</sup> and at least one dissenting opinion stated that if GIPSA developed regulation explaining whether a showing of competitive injury was required in a given circumstance, that regulation would entitle USDA to deference.<sup>27</sup> Amending § 201.3 with the addition of § 201.3(a) provides a structural foundation for the development of more specific regulations containing examples or criteria GIPSA may then use to determine if given conduct or action requires a showing of competitive injury or the potential for competitive injury to allege a violation of section 202(a) or section 202(b). As mentioned in the summary of comments, implementation of these specific regulations may lower costs to some livestock producers, swine production contract growers and poultry growers should they bring legal action for an alleged violation of section 202(a) or section 202(b). GIPSA acknowledges that § 201.3(a) may initially encourage litigation, temporarily driving up overall costs for stakeholders. While this interim rule is a standalone rulemaking, it is worth noting that GIPSA's current thinking is also expressed in separate proposed rules published concurrently in this edition of the **Federal Register**. GIPSA is proposing § 201.210, which clarifies the conduct or action by packers, swine contractors, or live poultry dealers that GIPSA considers unfair, unjustly discriminatory, or deceptive and a violation of section 202(a), and clarifies whether a showing of harm to competition or likelihood of harm to competition is required. GIPSA is also proposing § 201.211, which identifies criteria the Secretary will consider in determining whether conduct or action by packers, swine contractors, or live poultry dealers constitutes an undue or unreasonable preference or advantage and a violation of section 202(b). Section 201.214, as proposed in this edition of the **Federal**

**Register**, lists criteria the Secretary will consider in determining whether a live poultry dealer has used a poultry grower ranking system to compensate poultry growers in an unfair, unjustly discriminatory, or deceptive manner in violation of section 202(a), or in a way that gives an undue or unreasonable preference or advantage to any poultry grower or subjects any poultry grower to an undue or unreasonable prejudice or disadvantage in violation of section 202(b). GIPSA believes §§ 201.210, 201.211, and 201.214, once published as final rules, will mitigate potential costs associated with § 201.3(a) by clarifying what conduct or action would violate section 202(a) and section 202(b). Listing examples and criteria to explain the boundaries for compliance with section 202 of the P&S Act will promote compliance and reduce the number of disputes associated with section 202. Even while proposed §§ 201.210, 201.211, and 201.214 are being considered through the rulemaking process, amending § 201.3 with the addition of § 201.3(a) provides sufficient clarity to obtain deference from the courts.

#### VI. Required Impact Analyses

##### A. Executive Order 12866 and Regulatory Flexibility Act

This rulemaking has been determined to be "economically significant" for the purposes of Executive Order 12866 and, therefore, has been reviewed by the Office of Management and Budget. GIPSA is issuing this interim final rule under the P&S Act, in part, to formalize USDA's position that, in some cases, a violation of section 202(a) or (b) can be proven without proof of competitive injury or likelihood of competitive injury. As a required part of the regulatory process, GIPSA prepared an economic analysis of § 201.3(a). The first section of the analysis is an introduction and a discussion of the prevalence of contracting in the cattle, hog, and poultry industries as well as a discussion of potential market failures. Next, GIPSA discusses three regulatory alternatives it considered and presents a summary cost-benefit analysis of each alternative. GIPSA then discusses the impact on small businesses.

##### Introduction

GIPSA issued a proposed rule on June 22, 2010, which included §§ 201.3, 201.210, 201.211, 201.214. GIPSA is issuing amendments to § 201.3 as an interim final rule and is proposing new versions of §§ 201.210 and 201.211 in a separate proposed rule published concurrently in this issue of the **Federal**

**Register**. Likewise, 201.214 is being proposed in a separate rulemaking. Section 201.3(a) formalizes GIPSA's longstanding position that conduct or action can be found to violate sections 202(a) and/or 202(b) of the P&S Act without a finding of harm or likely harm to competition. GIPSA believes the interim final § 201.3(a) will serve to strengthen the protection afforded the nation's livestock producers and poultry growers.

Section 201.3(a) states that a finding that the challenged conduct or action adversely affects or is likely to adversely affect competition is not necessary in all cases . . . Some unfair, unjustly discriminatory, or deceptive practices do not result in competitive harm to the industry but still result in significant harm to individual livestock producers, swine production contract growers, and poultry growers. If, for example, a livestock producer, swine production contract grower, or poultry grower filed a complaint related to a matter that does not result in competitive harm, such as retaliatory conduct, use of inaccurate scales, or providing a poultry grower sick birds, the livestock producer, swine production contract grower, or poultry grower will be able to prevail without proof of harm to competition or the likelihood of harm to competition. GIPSA believes the standard articulated in § 201.3(a) is consistent with its mission, which is to "protect fair trade practices, financial integrity and competitive markets for livestock, meats and poultry."<sup>28</sup> By removing the burden to prove harm or likely harm to competition in all cases, this interim final rule promotes fairness and equity in the livestock and poultry industries.

Section 201.3(a) may lower the costs to some livestock producers, swine production contract growers, and poultry growers should they bring legal action for an alleged violation of sections 202(a) and/or 202(b). However, § 201.3(a) may initially increase litigation costs for the livestock and poultry industries while precedent setting decisions are established. While this interim rule is a standalone rulemaking, it is worth noting that GIPSA's current thinking is also expressed in separate proposed rules, which will clarify to the industry the types of conduct and criteria that GIPSA believes violate section 202(a) and section 202(b) of the P&S Act.

Proposed § 201.210(a) specifies that any conduct or action by a packer, swine contractor, or live poultry dealer that is explicitly deemed to be an

<sup>26</sup> *Wheeler v. Pilgrim's Pride Corp.*, 591 F.3d 355(5th Cir. 2009) (9–7 decision *en banc*) (Judge Garza dissenting, joined by Judges Jolly, Barksdale, Dennis, Prado, Elrod and Haynes).

<sup>27</sup> *Been v. O.K. Indus., Inc.*, 495 F.3d 1217, 1238 (10th Cir. 2007).

<sup>28</sup> [https://www.gipsa.usda.gov/laws/law/PS\\_act.pdf](https://www.gipsa.usda.gov/laws/law/PS_act.pdf). Accessed on September 19, 2016.

“unfair,” “unjustly discriminatory,” or “deceptive” practice or device by the P&S Act is a per se violation of section 202(a). Section 201.210(b) provides examples of conduct or action that, absent demonstration of a legitimate business justification, are “unfair,” “unjustly discriminatory,” or “deceptive” and a violation of section 202(a) regardless of whether the conduct or action harms or is likely to harm competition. Section 201.210(c) specifies that any conduct or action that harms or is likely to harm competition is an “unfair,” “unjustly discriminatory,” or “deceptive” practice or device and a violation of section 202(a). Many of the examples provided in § 201.210(b) relate to conduct or action that limits, by contract, the legal rights and remedies afforded by law to poultry growers, swine production contract growers, and livestock producers. Other examples specify conduct or actions that violate section 202(a).

As required by the 2008 Farm Bill, proposed § 201.211 specifies criteria the Secretary will consider when determining whether an undue or unreasonable preference or advantage has occurred in violation of section 202(b). The first four (4) criteria require the Secretary to consider whether one or more livestock producers, swine production contract growers, or poultry growers is treated more favorably as compared to other similarly situated livestock producers, swine production contract growers, or poultry growers. The fifth criterion in § 201.211 requires the Secretary to consider whether the packer, swine contractor, or live poultry dealer has demonstrated a legitimate business justification for conduct or action that may otherwise be an undue or unreasonable preference or advantage.

Proposed §§ 201.210 and 201.211 will thus limit the application of § 201.3(a)

by placing some parameters on conduct or action that constitutes unfair, unjustly discriminatory, and deceptive practices or devices under section 202(a), and on conduct or action that constitutes undue or unreasonable preferences or advantages under section 202(b). Proposed §§ 201.210 and 201.211 focus heavily on contracts between livestock producers and packers, swine production contract growers and swine contractors, and poultry growers and live poultry dealers.

While proposed §§ 201.210 and 201.211 focus heavily on contracts, § 201.3(a) is broad in nature. It applies to the use of all types of livestock and poultry procurement and growing arrangements by packers, swine contractors, and live poultry dealers, including packers’ use of negotiated cash purchases of livestock. As discussed below, contracting broadly defined, is the primary method by which livestock are procured (especially for hogs) and the almost exclusive arrangement under which poultry are produced. A discussion of contracting in these industries is, therefore, useful in explaining the need for § 201.3(a) and laying the foundation for the economic analysis of 201.3(a).

Prevalence of Contracting in Cattle, Hog, and Poultry Industries

Contracting is an important and prevalent feature in the production and marketing of livestock and poultry. Although § 201.3(a) applies to the livestock and poultry industries in general, proposed §§ 201.210 and 201.211 primarily affect livestock and poultry grown or marketed under contract. For example, under § 201.210(b)(2), absent demonstration of a legitimate business justification, GIPSA considers conduct or action by packers, swine contractors, or live poultry dealers that limit or attempt to

limit, by contract, the legal rights and remedies of livestock producers, swine production contract growers, or poultry growers as unfair, unjustly discriminatory, or deceptive and a violation of section 202(a) regardless of whether the conduct or action harms or is likely to harm competition. Section 201.211 defines criteria for section 202(b) violations with respect to providing undue or unreasonable preferences or advantages to one or more livestock producers or contract growers as compared to other livestock producers or contract growers.

The type of contracting varies among cattle, hogs, and poultry. Broilers, the largest segment of poultry, are almost exclusively grown under production contracts, while a small percentage of cattle are custom fed and shipped directly for slaughter this activity is not subject to the jurisdiction of the P&S Act. Hog production falls between these two extremes. As shown in Table 1 below, over 96 percent of all broilers are grown under contractual arrangements and over 40 percent of all hogs are grown under contractual arrangements. Live poultry dealers typically own the broilers and provide the growers with feed and medications. Contract growers provide the housing, labor, water, electricity and fuel to grow the birds. Similarly, swine contractors typically own the slaughter hogs and sell the finished hogs to pork packers. The swine contractors typically provide feed and medication to the contract growers who own the growing facilities and provide growing services. With the exception of turkey production, the use of contract growing arrangements has remained relatively stable over the years that the Census of Agriculture has published data on commodities raised and delivered under production contracts as Table 1 shows.

TABLE 1—PERCENTAGE OF POULTRY AND HOGS RAISED AND DELIVERED UNDER PRODUCTION CONTRACTS<sup>29</sup>

Species	2002	2007	2012
Broilers .....	98.0	96.5	96.4
Turkeys .....	41.7	67.7	68.5
Hogs .....	42.9	43.3	43.5

Another contract category is marketing contracts, where producers market their livestock to a packer for slaughter under a verbal or written agreement. These are commonly referred to as Alternative Marketing

Arrangements (AMAs). Pricing mechanisms vary across AMAs. Some AMAs rely on a spot market for at least one aspect of its price, while others involve complicated pricing formulas with premiums and discounts based on

carcass merits. The livestock seller and packer agree on a pricing mechanism under AMAs, but usually not on a specific price.

USDA’s Agricultural Marketing Service (AMS) reports the number of

<sup>29</sup> Agricultural Census, 2007 and 2012. [https://www.agcensus.usda.gov/Publications/2012/Full\\_](https://www.agcensus.usda.gov/Publications/2012/Full_)

[Report/Volume\\_1\\_Chapter\\_1\\_US/](https://www.agcensus.usda.gov/Publications/2007/Full_Report/Volume_1_Chapter_1_US/) and [https://www.agcensus.usda.gov/Publications/2012/Full\\_](https://www.agcensus.usda.gov/Publications/2012/Full_Report/Volume_1_Chapter_1_US/)

[www.agcensus.usda.gov/Publications/2007/Full\\_Report/Volume\\_1\\_Chapter\\_1\\_US/](https://www.agcensus.usda.gov/Publications/2007/Full_Report/Volume_1_Chapter_1_US/)



cattle sold to packers under formula, forward contract, and negotiated pricing mechanisms. The following table illustrates the prevalence of contracting in the marketing of fed cattle.

TABLE 2—PERCENTAGE OF FED CATTLE SOLD BY TYPE OF PURCHASE<sup>30</sup>

Year	Formula	Forward contract	Negotiated
2005	30.4	5.0	64.6
2006	31.5	6.8	61.7
2007	33.2	8.3	58.5
2008	37.4	9.9	52.7
2009	43.7	7.0	49.3
2010	44.9	9.5	45.6
2011	48.4	10.9	40.7
2012	54.7	11.4	33.8
2013	60.0	10.2	29.8
2014	58.1	14.2	27.6
2015	58.2	16.5	25.3

GIPSA considers cattle sold under formula pricing methods as sold under AMA contracts. Thus, the first two columns in the above table are cattle marketed under contract and the third column represents the spot market for fed cattle. The data in the table above show that the contracting of cattle has increased significantly since 2005.

Approximately 35 percent of fed cattle were marketed under contracts in 2005. By 2015, the percentage of fed cattle marketed to packers under contracts had increased to almost 75 percent, while negotiated spot market transactions have decreased to about 25 percent of all transactions.

As discussed above, over 40 percent of hogs are grown under production

contracts. These hogs are then sold by swine contractors to packers under marketing contracts. The prevalence of marketing contracts in the sale of finished hogs, which includes production contract and non-production contract hogs, to packers is even more prevalent as shown in the table below.

TABLE 3—PERCENTAGE OF HOGS SOLD BY TYPE OF PURCHASE<sup>31</sup>

Year	Other marketing arrangements <sup>32</sup>	Formula <sup>33</sup>	Negotiated
2005	39.3	49.7	11.0
2006	44.0	46.4	9.6
2007	44.8	46.5	8.7
2008	43.9	47.6	8.5
2009	42.8	50.4	6.8
2010	45.4	49.4	5.2
2011	47.6	48.2	4.2
2012	47.7	48.6	3.6
2013	48.3	48.4	3.2
2014	45.9	51.4	2.7
2015	46.0	51.4	2.6

Similar to cattle, the percentage of hogs sold under marketing contracts has increased since 2005 to over 97 percent in 2015. The spot market for hogs has declined to 2.6 percent in 2015. As these data demonstrate, almost all hogs are marketed under some type of marketing contract.

#### Benefits of Contracting in Cattle, Hog, and Poultry Industries

Contracts have many benefits. They help farmers and livestock producers manage price and production risks,

elicit the production of products with specific quality attributes by tying prices to those attributes, and smooth the flows of commodities to processing plants encouraging more efficient use of farm and processing capacities. Agricultural contracts can also lead to improvements in efficiency throughout the supply chain for products by providing farmers with incentives to deliver products consumers desire and produce products in ways that reduce processing costs and, ultimately, retail prices.

In 2007, RTI International conducted a comprehensive study of marketing practices in the livestock and red meat industries from farmers to retailers (the RTI Study).<sup>34</sup> The RTI Study analyzed the extent of use, price relationships, and costs and benefits of contracting, including AMAs. The RTI Study found that AMAs increased the economic efficiency of the livestock markets and yielded economic benefits to consumers, producers and packers.

The RTI Study found that efficiencies come from less volatility in volume and

<sup>30</sup> USDA's Agricultural Marketing Service. <https://mpr.datamart.ams.usda.gov/menu.do?path=Products\Cattle\Weekly>. Accessed on September 9, 2016

<sup>31</sup> USDA's Agricultural Marketing Service.

<sup>32</sup> Includes Packer Owned and Packer Sold, Other Purchase Arrangements.

<sup>33</sup> Includes Swine Pork Market Formula, Other Market Formula.

<sup>34</sup> RTI International, 2007, GIPSA Livestock and Meat Marketing Study, Prepared for GIPSA.



more intensive use of production and processing facilities, meaning less capital, labor, feed, and materials per pound of meat produced. Efficiencies also come from reduced transaction costs and from sending price signals to better match the meat attributes to consumer demand. Consumers benefit from lower meat prices and meat with desired attributes. In turn, the consumer benefits increase livestock demand, which provides benefits to producers.

Structural Issues in the Cattle, Hog, and Poultry Industries

As the above discussion highlights, there are important benefits associated with the use of agriculture contracts in the cattle, hog, and poultry industries. However, if there are large disparities in the bargaining power among contracting

parties resulting from size differences between contracting parties or the use of market power by one of the contracting parties, the contracts may have detrimental effects on one of the contracting parties and may result in inefficiencies in the marketplace.

For example, a contract that ties a grower to a single purchaser of a specialized commodity or service, even if the contract provides for fair compensation to the grower, still leaves the grower subject to default risks should the contractor fail. Another example is a contract that covers a shorter term than the life of the capital (a poultry house, for example). The grower may face the hold-up risk that the contractor may require additional capital investments or may impose lower returns at the time of contract

renewal. Hold-up risk is a potential market failure and is discussed in detail in the next section. These risks may be heightened when there are no alternative buyers for the grower to switch to, or when the capital investment is specific to the original buyer.<sup>35</sup> Some growers make substantial long-term capital investments as part of livestock or poultry production contracts, including land, poultry or hog houses, and equipment. Those investments may tie the grower to a single contractor or integrator. Costs associated with default risks and hold-up risks are important to many growers in the industry. The table below shows the number of integrators that broiler growers have in their local areas by percent of total farms and by total production.

TABLE 4—INTEGRATOR CHOICE FOR BROILER GROWERS<sup>36</sup>

Integrators in grower's area <sup>37</sup>	Percent of total			Can change to another integrator (percent of farms)
	Farms	Birds	Production	
Number:				
1 .....	21.7	23.4	24.5	7
2 .....	30.2	31.9	31.7	52
3 .....	20.4	20.4	19.7	62
4 .....	16.1	14.9	14.8	71
>4 .....	7.8	6.7	6.6	77
No Response .....	3.8	2.7	2.7	Na

The data in the table show that 52 percent of broiler growers, accounting for 56 percent of total production, report having only one or two integrators in their local areas. This limited integrator choice may accentuate the contract risks. A 2006 survey indicated that growers facing a single integrator received 7 to 8 percent less compensation, on average, than farmers located in areas with 4 or more integrators.<sup>38</sup> If live poultry dealers already possess some market power to force prices for poultry growing services below competitive levels, some contracts can extend that power by raising the costs of entry for new competitors, or allowing for price discrimination.<sup>39</sup>

Many beef, pork, and poultry processing markets face barriers to entry, including: (1) Economies of scale;

(2) high asset-specific capital costs with few alternative uses of the capital; (3) brand loyalty of consumers, customer loyalty to the incumbent processors, and high customer switching costs; and (4) governmental food safety, bio-hazard, and environmental regulations. Consistent with these barriers, there has been limited new entry.

However, an area where entry has been successful is in developing and niche markets, such as organic meat and free-range chicken. Developing and niche markets have a relatively small consumer market that is willing to pay higher prices, which supports smaller plant sizes. Niche processors are generally small, however, and do not offer opportunities to many producers or growers.

Economies of scale have resulted in large processing plants in the beef, pork,

and poultry processing industries. The barriers to entry discussed above may have limited the entry of new processors, which limits the expansion of choice of processors to which livestock producers market their livestock. Barriers to entry also limit the expansion of choice for poultry growers who have only one or two integrators in their local areas with no potential entrants on the horizon. The limited expansion of choice of processors by livestock producers, swine production contract growers, and poultry growers may limit contract choices and the bargaining power of producers and growers in negotiating contracts.

One indication of potential market power is industry concentration.<sup>40</sup> The following table shows the level of concentration in the livestock and

<sup>35</sup> See Vukina and Leegomonchai, *Oligopsony Power, Asset Specificity, and Hold-Up: Evidence From The Broiler Industry*, *American Journal of Agricultural Economics*, 88(3): 589–605 (August 2006).

<sup>36</sup> MacDonald, James M. Technology, Organization, and Financial Performance in U.S. Broiler Production. USDA, Economic Research Service, June 2014.

<sup>37</sup> Percentages were determined from the USDA Agricultural Resource Management Survey (ARMS),

2011. "Respondents were asked the number of integrators in their area. They were also asked if they could change to another integrator if they stopped raising broilers for their current integrator." *Ibid.* p. 30

<sup>38</sup> MacDonald, J. and N. Key. "Market Power in Poultry Production Contracting? Evidence from a Farm Survey." *Journal of Agricultural and Applied Economics*. 44(4) (November 2012): 477–490.

<sup>39</sup> See, for example, Williamson, Oliver E. *Markets and Hierarchies: Analysis and Antitrust*

*Implications*, New York: The Free Press (1975); Edlin, Aaron S. & Stefan Reichelstein (1996) "Holdups, Standard Breach Remedies, and Optimal Investment," *The American Economic Review* 86(3): 478–501 (June 1996).

<sup>40</sup> For additional discussion see MacDonald, J.M. 2016 "Concentration, contracting, and competition policy in U.S. agribusiness," *Competition Law Review*, No. 1–2016: 3–8.

poultry slaughtering industries for 2005–2015.

TABLE 5—FOUR-FIRM CONCENTRATION IN LIVESTOCK AND POULTRY SLAUGHTER<sup>41</sup>

Year	Steers & heifers (%)	Hogs (%)	Broilers (%)	Turkeys (%)
2005	80	64	n.a.	n.a.
2006	81	61	n.a.	n.a.
2007	80	65	57	52
2008	79	65	57	51
2009	86	63	53	58
2010	85	65	51	56
2011	85	64	52	55
2012	85	64	51	53
2013	85	64	54	53
2014	83	62	51	58
2015	85	66	51	57

The table above shows the concentration of the four largest steer and heifer slaughterers has remained relatively stable between 79 and 86 percent since 2005. Hog and broiler slaughter concentration has also remained relatively steady at over 60 percent and 50 percent, respectively.

The data in Table 5 are estimates of national concentration and the size differences discussed below are also at the national level, but the economic markets for livestock and poultry may be regional or local, and concentration in regional or local areas may be higher than national measures. For example, while poultry markets may appear to be the least concentrated in terms of the four-firm concentration ratios presented above, economic markets for poultry growing services are more localized than markets for fed cattle or hogs, and local concentration in poultry markets is greater than in hog and other livestock markets.<sup>42</sup> The data presented earlier in Table 4 highlight this issue by showing the limited ability a poultry grower has to switch to a different integrator. As a result, national concentration may not demonstrate accurately the options poultry growers in a particular region actually face.

Empirical evidence does not show a strong or simple relationship between increases in concentration and increases in market power. Other factors matter, including the ease of entry by new producers into a concentrated industry and the ease with which retail food buyers or agricultural commodity sellers can change their buying or marketing

strategies in response to attempts to exploit market power.

For example, in 2009, the Government Accountability Office (GAO) reviewed 33 studies published since 1990 that were relevant for assessing the effect of concentration on commodity or food prices in the beef, pork, or dairy sectors.<sup>43</sup> Most of the studies found no evidence of market power, or found that the efficiency gains from concentration were larger than the market power effects. Efficiency gains would be larger if increased concentration led to reduced processing costs (likely to occur if there are scale economies<sup>44</sup> in processing), and if the reduced costs led to a larger effect on prices than the opposing impact of fewer firms. For example, with respect to beef processing, the GAO report concluded that concentration in the beef processing sector has been, overall, beneficial because the efficiency effects dominated the market power effects, thereby reducing farm-to-wholesale beef margins.

Several studies reviewed by the GAO did find evidence of market power in the retail sector, in that food prices exceeded competitive levels or that commodity prices fell below competitive levels. However, the GAO study also concluded that it was not clear whether market power was caused by concentration or some other factor. In interviews with experts, the GAO report concluded that increases in concentration may raise greater concerns in the future about the potential for market power and the

manipulation of commodity or food prices.

Another factor GIPSA considered in proposing §§ 201.210 and 201.211 is the contrast in size and scale between livestock producers, swine production contract growers, and poultry growers and the packers, swine contractors, and live poultry dealers they supply. The disparity in size between large oligopsonistic buyers and atomistic sellers may lead to market power and asymmetric information. The 2012 Census of Agriculture reported 740,978 cattle and calf farms with 69.76 million head of cattle for an average of 94 head per operation. Ninety-one percent of these were family or individually-owned operations.<sup>45</sup> The largest one percent of cattle farms sold about 51 percent of the cattle sold by all cattle farms.

There were 33,880 cattle feeding operations in 2012 that sold 25.47 million head of fed cattle for an average of 752 head per feedlot. The 607 largest feedlots sold about 75 percent of the fed cattle, and averaged 32,111 head sold. About 80 percent of feedlots were family or individually owned.<sup>46</sup> As Table 5 shows, the four largest cattle packers processed about 85 percent, 25.47 million head, for an average of 5.41 million head per cattle packer. This means the average top four cattle packers had 57,574 times the volume of the average cattle farm, and 1,054 times the volume of the largest one percent of cattle farms. It also means the average top four cattle packers had 7,197 times the volume of the average feedlot, and

<sup>41</sup> The data on cattle and hogs were compiled from USDA's NASS data of federally inspected slaughter plants. Data on broilers and turkeys were compiled from Packers and Stockyards industry annual reports. Both data sources are proprietary.

<sup>42</sup> MacDonald and Key (2012) Op. Cit. and Vukina and Leegomonchai (2006) Op. Cit.

<sup>43</sup> United States Government Accountability Office. Concentration in Agriculture. GAO-09-746R. Enclosure II: Potential Effects of

Concentration on Agricultural Commodity and Retail Food Prices.

<sup>44</sup> Scale economies are present when average production costs decrease as output increases.

<sup>45</sup> Census of Agriculture, 2012.

<sup>46</sup> Ibid.

169 times the volume of the very largest feedlots.

The USDA, National Agricultural Statistics Service 2012 livestock slaughter summary reported that in 2012, 113.16 million head of hogs were commercially slaughtered in the United States.<sup>47</sup> Table 5 shows that the top four hog packers processed about 64 percent of those hogs, which comes to an average of about 18.1 million head of hogs per top four packer. The 2012 Census of Agriculture reported 55,882 farms with hog and pig sales.<sup>48</sup> About 83 percent of the farms were family or individually owned. Of the 55,882 farms with hog and pig sales, 47,336 farms were independent growers raising hogs and pigs for themselves (sold an average of 1,931 head), 8,031 were swine production contract growers raising hogs and pigs for someone else (an average of 10,970 head per swine production contract grower), and 515 were swine contractors (sold an average of 38,058 head per swine contractor).<sup>49</sup>

The National Chicken Council states that in 2016, approximately 35 companies were involved in the business of raising, processing, and marketing chicken on a vertically integrated basis, while about 25,000 family farmers had production contracts with those companies.<sup>50</sup> That comes to about 714 family-growers per company. Collectively, the family-growers produced about 95 percent of the nearly 9 billion broilers produced in the United States in 2015. The other 5 percent were grown on company-owned farms. That means the average family-grower produced about 342,000 broilers. As Table 5 shows, the four largest poultry companies in the United States accounted for 51 percent of the broilers processed. That means the average volume processed by the four largest poultry companies was about 1.15 billion head, which was 3,357 times the average family grower's volume.

As the above discussion highlights, there are large size differences between livestock producers and meat packers. There are also large size differences between poultry growers and the live poultry dealers which they supply. These size differences may contribute to unequal bargaining power due to monopsony market power or oligopsony market power, or asymmetric information. The result is that the contracts bargained between the parties

may have detrimental effects on livestock producers, swine production contract growers, and poultry growers due to the structural issues discussed above and may result in inefficiencies in the marketplace.

#### Hold-Up as a Potential Market Failure

Integrators demand investment in fixed assets from the growers. One example is specific types of poultry houses and equipment the integrator may require the grower to utilize in their growing operations. These investments may improve efficiency by more than the cost of installation. Typically, the improved efficiency would accrue to both the integrator and the grower. The integrator has lower feed costs, and the grower performs better relative to other poultry growers in a settlement group. If the grower bears the entire cost of installation, then the grower should be further compensated for the feed conversion gains that accrue to the integrator. The risk is that after the assets are installed, the cost to the grower is "sunk." This means that if the integrator reneges on paying compensation for the additional capital investments, and insists on maintaining the lower price, the grower will accept that lower price rather than receive nothing. This allows the integrator to get the benefit of the efficiency gains, at no expense to them, with the grower bearing all of the cost. This renegeing is termed "hold-up" in the economic literature.<sup>51</sup>

Hold-up can have two consequences that result in a misallocation of resources. If the growers do not anticipate hold-up, then growers will spend too much on investments because the integrator who demands them is not incurring any cost. That is inefficient. If the grower does anticipate hold-up, they will act as if the integrator were going to renege even when they were not, resulting in too little investment and a loss of potential efficiency gains.

Hold-up can be resolved with increased competition. If an integrator developed a reputation for reneging, and growers could go elsewhere, the initial integrator would be punished and disincentivized from reneging in the future. Unfortunately, in practice, many growers do not have the option of going elsewhere.

Data shown above in Table 4 indicate that there are few integrators in these markets, and that growers have limited choice. Table 5, above, indicates the

level of concentration in the livestock and poultry slaughtering industries and shows that integrators and livestock packers operate in concentrated markets.

This rule would allow growers to file complaints against integrators that renege, giving some of the incentive benefit of competition, without compromising the efficiency of having a few large processors.

#### Contracting, Industry Structure, and Market Failure: Summary of the Need for Regulation

There are benefits of contracting in the livestock and poultry industries, as well as structural issues that may result in unequal bargaining power and market failures. These structural issues and market failures will be mitigated by relieving plaintiffs from the requirement to demonstrate competitive injury. For instance, contracting parties can alleviate hold-up problems if they are able to write complete contracts, and are able to litigate to enforce the terms of those contracts when there is an attempt to engage in ex-post hold-up. Because proving competitive injury is difficult and costly, removing that burden will facilitate the use of litigation by producers and growers to address violations of the Packers and Stockyards Act. If growers are able to seek legal remedies, then their contracts are easier to enforce. This will incentivize packers, swine contractors, and integrators to avoid exploitation of market power and asymmetric information, as well as behaviors that result in the market failure of hold-up. The result will be improved efficiency in the livestock and poultry markets.

GIPSA has a clear role to ensure that market failures are mitigated so that livestock and poultry markets remain fair and competitive. Section 201.3(a) seeks to fulfill that role by promoting fairness and equity for livestock producers, swine production contract growers, and poultry growers.

#### Costs of the Regulations Proposed on June 22, 2010

GIPSA issued a proposed rule on June 22, 2010, which included §§ 201.3, 201.210, and 201.211. GIPSA received and considered thousands of comments before finalizing § 201.3(a) and before proposing the current versions of §§ 201.210, and 201.211. The following provisions were proposed in 2010 but are not in § 201.3 or currently proposed §§ 201.210 and 201.211.

- Applicability to all stages of a live poultry dealer's poultry production, including pullets, laying hens, breeders, and broilers (§ 201.3(a)).

<sup>47</sup> Ibid.

<sup>48</sup> A pig is a generic term for a young hog.

<sup>49</sup> Agricultural Census, 2012.

<sup>50</sup> <http://www.nationalchickencouncil.org/about-the-industry/statistics/broiler-chicken-industry-key-facts/>.

<sup>51</sup> See for example, Benjamin Klein, Robert G. Crawford, and Armen A. Alchian, "Vertical Integration, Appropriate Rents, and the Competitive Contracting Process," *The Journal of Law and Economics* 21, no. 2 (Oct., 1978): 297–326.

- Applicability to all swine production contracts, poultry growing arrangements and livestock production and marketing contracts, including formula and forward contracts (§ 201.3(b)).

- Requirement that packers, live poultry dealers, and swine contractors maintain records justifying differences in prices (§ 201.210(a)(5)).
- Provision prohibiting packers from purchasing livestock from other packers (§ 201.212(c)).

- Requirement that packers offer the same terms to groups of small producers as offered to large producers when the group can collectively meet the same quantity commitments (§ 201.211(a)).

- Requirement that packers refrain from entering into exclusive agreements with livestock dealers (§ 201.212(b)).

- Requirements that packers and live poultry dealers submit sample contracts to GIPSA for posting to the public (§ 201.213).

Although many thousands of the comments submitted contained general qualitative assessments of either the costs or benefits of the proposed rule, only two comments systematically described quantitative costs across the rule provisions. Comments from the National Meat Association (NMA) included cost estimates by Informa Economics (the Informa Study). The Informa Study projected costs of \$880 million, \$401 million, and \$362 million for U.S. cattle and beef, hogs and pork, and poultry industries respectively.<sup>52</sup> However, these cost estimates were for all of the 2010 proposed changes, many of which do not apply. The Informa Study estimated \$133.3 million to be one-time direct costs resulting from rewriting contracts, additional record keeping, etc.<sup>53</sup> The majority of the costs would be indirect costs. The Informa Study estimated \$880.9 million in costs due to efficiency losses and \$459.9 million in costs due to reduced demand caused by a reduction in meat quality resulting from fewer AMAs.

Comments from the National Chicken Council (NCC) included cost estimates prepared by Dr. Thomas E. Elam, President, FarmEcon LLC (the Elam Study).<sup>54</sup> The Elam Study estimated that the entire 2010 proposed rule would cost the chicken industry \$84 million in the first year increasing to \$337 million in the fifth year, with a total cost of

\$1.03 billion over the first five years.<sup>55</sup> The Elam Study identified \$6 million as one-time administrative costs. Most of the costs would be indirect costs resulting from efficiency losses.<sup>56</sup> More than half of the costs would be due to a reduced rate of improvement in feed efficiency. Again, these cost estimates were for all of the 2010 proposed changes, many of which do not apply.

The Informa Study estimated that the proposed provision requiring packers to refrain from entering into exclusive agreements with livestock dealers would cost livestock auctions as much as \$85.5 million.<sup>57</sup> Because GIPSA has no current plans to propose the “exclusive agreements” rule, those costs no longer apply. The Informa Study did not directly specify how much the estimates in the study attributed to each of the other provisions, but GIPSA expects that their omission will substantially reduce the cost of § 201.3(a).

Estimates of the costs in the Informa Study and the Elam Study were largely due to projections that packers, swine contractors, and live poultry dealers, would alter business practices in reaction to the proposed rule. For example, the Informa Study projected that packers would reduce the number and types of AMAs to avoid potential litigation,<sup>58</sup> and the Elam Study expected live poultry dealers to evaluate each load of feed delivered to growers to avoid litigation.<sup>59</sup>

The estimates from the Informa Study and the Elam Study may overstate costs because the studies relied on interviews of packers, swine contractors, live poultry dealers, and other stakeholders for much of the basis for the estimates of the willingness of packers, swine contractors, and live poultry dealers to alter their business practices. Moreover, neither study considered benefits from the proposed rule.

The Informa Study projected that the regulations proposed in 2010 would cause beef and pork packers to limit their involvement in vertical arrangements, and without those arrangements, they would not be able to produce the branded products they currently offer. The Informa Study projected that, as a result, beef and pork markets would lose \$460 million, which is about half of the value added from branded products.<sup>60</sup>

GIPSA does not expect that the current § 201.3(a) would cause beef and pork markets to abandon half of the value added from branded products. Current § 201.3(a) does not prevent packers from offering quality incentives to hog or cattle feeders, and any vertical coordination among feeders and producers would be outside of GIPSA’s jurisdiction.

Given the differences from the rule proposed in 2010, the estimates from the Elam Study likely overstated the costs of compliance to the poultry industry with current § 201.3(a) by at least \$115 million over five years. The Informa Study estimates would overstate costs of compliance to the cattle, hog, and poultry industries with current § 201.3(a) by at least \$500 million. If packers, swine contractors, and live poultry dealers overstated their willingness to alter their business practices, then the estimates could be overstated that much more.

#### Cost-Benefit Analysis of § 201.3(a) Regulatory Alternatives Considered

Executive Order 12866 requires an assessment of costs and benefits of potentially effective and reasonably feasible alternatives to the planned regulation and an explanation of why the planned regulatory action is preferable to the potential alternatives.<sup>61</sup> GIPSA considered three regulatory alternatives. The first alternative that GIPSA considered is the baseline to maintain the status quo and not finalize § 201.3(a). The second alternative that GIPSA considered is to issue § 201.3(a) as an interim final regulation. This is GIPSA’s preferred alternative as will be explained below. The third alternative that GIPSA considered is issuing § 201.3(a) as an interim final regulation, but exempting small businesses, as defined by the Small Business Administration, from having to comply with the regulation.

#### Regulatory Option 1: Status Quo

If § 201.3(a) is never finalized, there are no marginal costs and marginal benefits as industry participants will not alter their conduct. From a cost standpoint, this is the least cost alternative compared to the other two alternatives. This alternative also has no marginal benefits. Since there are no changes from the status quo under this regulatory alternative, it will serve as the baseline against which to measure the other two alternatives.

<sup>61</sup> See Section 6(a)(3)(C) of Executive Order 12866.

<sup>52</sup> Informa Economics, Inc. “An Estimate of the Economic Impact of GIPSA’s Proposed Rules,” prepared for the National Meat Association, 2010, Table 10, Page 53.

<sup>53</sup> Ibid. Page 53.

<sup>54</sup> See Elam, Dr. Thomas E. “Proposed GIPSA Rules Relating to the Chicken Industry: Economic Impact.” FarmEcon LLC, 2010.

<sup>55</sup> Ibid. Page 24

<sup>56</sup> Ibid. Page 24.

<sup>57</sup> Ibid. Page 49.

<sup>58</sup> Informa, page 30.

<sup>59</sup> Elam, page 18.

<sup>60</sup> Informa, pages 51 and 52.

Regulatory Alternative 2: The Preferred Alternative

Section 201.3(a) states that conduct or action can be found to violate sections 202(a) and/or 202(b) of the P&S Act without a finding of harm or likely harm to competition. Given the applicability of the regulation to the entire livestock and poultry industries, it is difficult to predict how the industries will respond. Therefore, GIPSA believes that assigning a range to the expected costs of the regulation is appropriate.

At the lower boundary of the cost spectrum, GIPSA considers the scenario where the only costs are increased litigation costs and there are no adjustments by the livestock and poultry industries to reduce their use of AMAs or incentive pay systems, such as poultry grower ranking systems, and there are no changes to existing marketing or production contracts. For the upper boundary of the cost spectrum, GIPSA considers the scenario in which the livestock and poultry industries adjust their use of AMAs and incentive pay systems and makes systematic changes in its marketing and production contracts to reduce the threat of litigation.

A. Regulatory Alternative 2: Lower Boundary of Cost Spectrum—Litigation Costs of Preferred Alternative

GIPSA modeled the litigation costs by estimating the total cost of litigating a case filed under the jurisdiction of the P&S Act. The main costs are attorney fees to litigate a case in a court of law. Limited empirical data on actual historical litigation costs required GIPSA to use a cost engineering approach to estimate litigation costs. In considering the costs of the 2010

proposed rule, GIPSA, based on its expertise, assumed a cost of \$3.5 million to litigate a case. GIPSA uses the same starting point here. The cost of litigating a case includes the costs to all parties including the respondent and the USDA in a case brought by the USDA and the costs of the plaintiff and the defendant in the case of private litigation.

GIPSA then examined the actual number of cases decided under the P&S Act from 1926 to 2014. The listing of court decisions and the court in which the decision was reached came from the National Agricultural Law Center at the University of Arkansas.<sup>62</sup> GIPSA then reviewed each case and classified it as either competition, financial, or trade practice cases. This is an internal classification system corresponding to the types of violations GIPSA investigates.

All of the cases were assigned a specific attorney fee based on a random sample from a normal distribution ranging between \$250 thousand and \$3.5 million for trade practice cases, \$250 thousand to \$3 million for financial cases, and \$1.5 million to \$5 million for competition cases. These ranges are based on GIPSA’s expertise and the complexity of each type of case, with competition being the most complex and therefore the most costly to litigate. This expertise comes from GIPSA’s experience litigating each type of case and monitoring private litigation under the P&S Act. GIPSA estimated the cost of litigating each case from 1926 to 2014 using the cost ranges outlined above.

GIPSA scaled the initial cost up or down based on the court making the decision and based on GIPSA’s assumption that Supreme Court cases

are more expensive than District court cases, which are more expensive than state court cases. For Supreme Court cases, GIPSA scaled up the cost by a factor of three. For District court cases, GIPSA left the costs unchanged except for the sole case litigated in the United States District Court for the District of Columbia, which GIPSA scaled up by a factor of 1.1. GIPSA scaled state courts down by a factor of 0.7.

After estimating the cost of each case, by case type, GIPSA averaged all cases decided each year to obtain an estimated annual average cost of litigation. GIPSA then conducted a Monte Carlo simulation by sampling from a normal distribution of estimated average annual litigation costs for each type of case to arrive at the final estimated annual average cost of litigating cases filed under the P&S Act.<sup>63</sup>

GIPSA recognizes the uncertainty in estimating litigation costs and conducted sensitivity analysis using a Monte Carlo simulation on the estimated average annual litigation costs. GIPSA used a normal distribution of estimated litigation costs and calculated estimated litigation costs at the 2.5th percentile (lower percentile) of the distribution, the mean (average), and the 97.5th percentile (upper percentile).

GIPSA then estimated a linear trend line through the data using the Ordinary Least Squares (OLS) linear regression technique and used the trend line to project the litigation costs for 2015–2017.<sup>64</sup> These are baseline litigation costs that GIPSA expects to occur without the regulation. The table below shows the estimated and projected baseline litigation costs for 2007–2017.<sup>65</sup>

TABLE 6—ESTIMATED AND PROJECTED BASELINE LITIGATION COSTS FOR 2007–2017<sup>66</sup>

Year	Lower percentile (\$ millions)	Average (\$ millions)	Upper percentile (\$ millions)
2007	4.98	8.88	12.77
2008	2.16	5.12	8.08
2009	8.45	13.00	17.46
2010	6.82	11.25	15.60
2011	10.52	15.28	20.02
2012	6.49	10.10	13.81
2013	1.94	4.14	6.42
2014	3.56	6.74	10.03
2015	4.32	8.13	12.10
2016	4.45	8.28	12.31
2017	4.58	8.42	12.52

<sup>62</sup> <http://nationalaglawcenter.org/aglaw-reporter/case-law-index/packers-and-stockyards>. We note that this list is not exhaustive, but it is extensive.

<sup>63</sup> Monte Carlo simulation is a statistical technique that relies on repeated random sampling from a distribution to obtain numerical results.

<sup>64</sup> Ordinary least squares regression technique is a method for estimating the unknown parameters

using an established statistical model based on existing data observations.

<sup>65</sup> The baseline litigation costs are those costs GIPSA expects to occur without implementation of § 201.3(a).

GIPSA then reviewed the complete history of all investigations conducted by its Packers and Stockyards Program since 2009 and separated out the investigations involving alleged violations of sections 202(a) and 202(b) of the P&S Act for cattle, hogs, and poultry because § 201.3(a) only applies to alleged violations of sections 202(a)

and 202(b). The GIPSA investigation data are more robust, with more observations than the case data. There were never many cases in any given year. In addition, the data since 2009 are better predictors of the next ten years than cases that took place as far back as 1926.

Based on the history of investigations, GIPSA then allocated all of the projected baseline litigation costs for 2017 into section 202(a) and 202(b) violations for each species at the lower percentile, the average, and the upper percentile. These allocations appear in the tables below.

**TABLE 7—ALLOCATION OF § 201.3(a) BASELINE LITIGATION COSTS FOR 2017 AT THE LOWER PERCENTILE**

P&S Act section	Cattle (\$ millions)	Hog (\$ millions)	Poultry (\$ millions)	Total (\$ millions)
202(a) .....	1.00	0.65	2.01	3.66
202(b) .....	0.10	0.11	0.71	0.92
Total .....	1.10	0.76	2.72	4.58

**TABLE 8—ALLOCATION OF § 201.3(a) BASELINE LITIGATION COSTS FOR 2017 AT THE AVERAGE**

P&S Act section	Cattle (\$ millions)	Hog (\$ millions)	Poultry (\$ millions)	Total (\$ millions)
202(a) .....	1.84	1.20	3.70	6.73
202(b) .....	0.19	0.21	1.30	1.69
Total .....	2.02	1.41	4.99	8.42

**TABLE 9—ALLOCATION OF § 201.3(a) BASELINE LITIGATION COSTS FOR 2017 AT THE UPPER PERCENTILE**

P&S Act section	Cattle (\$ millions)	Hog (\$ millions)	Poultry (\$ millions)	Total (\$ millions)
202(a) .....	2.73	1.78	5.50	10.00
202(b) .....	0.28	0.31	1.93	2.52
Total .....	3.00	2.09	7.42	12.52

These allocations assume that all projected baseline litigation costs for 2017 will come only from section 202(a) and 202(b) violations. GIPSA then estimated the additional litigation costs the first full year the regulation is in place.

In order to estimate the additional expected litigation costs in 2017 assuming § 201.3(a) becomes effective in early 2017, GIPSA again utilized the complete history of all investigations conducted by its Packers and Stockyards Program since 2009. GIPSA based the additional litigation costs on the difference between the number of

complaints received in 2015 on alleged conduct that may violate sections 202(a) and 202(b), by species, and the highest number of complaints GIPSA received in any year since 2009. By 2015, court decisions had established the requirement to demonstrate harm to competition, which likely resulted in fewer complaints of Section 202(a) and 202(b) violations, particularly in the poultry industry, than in previous years when this requirement was not fully realized by industry participants. GIPSA expects § 201.3(a) will result in additional new complaints filed with GIPSA that will be at the levels

experienced between 2009 and 2015 before the requirement of harm to competition was fully realized. GIPSA tracks the number of complaints received through a complaint tracking system initiated in 2009. Thus, this difference, by species, is the increase in complaints GIPSA expects when the regulations are finalized. GIPSA then used these differences as scaling factors to estimate the litigation that GIPSA expects to occur in 2017, the first full year that § 201.3(a) becomes effective. The scaling factors appear in the table below:

**TABLE 10—SCALING FACTORS FOR LITIGATION FROM § 201.3(a)**

P&S Act section	Cattle	Hog	Poultry
202(a) .....	2.30	1.40	2.15
202(b) .....	2.30	1.20	2.15

<sup>66</sup> The litigation costs for 2007–2014 are estimated using Monte Carlo simulation at the lower percentile, the average, and the upper

percentile and 2015–2017 are projected using the estimated trend lines using OLS and historical

estimates. The cost of each case is measured using 2016 dollars.

The scaling factors run from 1.20 for hogs to 2.30 for cattle. To finalize the estimated increase in litigation costs, GIPSA multiplied the scaling factors in the above table by the projected 2017 baseline litigation costs

at the lower percentile, the average, and the upper percentile to arrive at the expected litigation costs in 2017. GIPSA then subtracted out the projected baseline litigation costs to arrive at the

estimated additional litigation costs that GIPSA expects to occur assuming § 201.3(a) become effective in early 2017. These estimated litigation costs appear in the following tables.

TABLE 11—PROJECTED § 201.3(a) LITIGATION COSTS FOR 2017 AT THE LOWER PERCENTILE

P&S Act section	Cattle (\$ millions)	Hog (\$ millions)	Poultry (\$ millions)	Total (\$ millions)
202(a) .....	1.30	0.26	2.31	3.87
202(b) .....	0.13	0.02	0.81	0.97
Total .....	1.43	0.28	3.12	4.84

TABLE 12—PROJECTED § 201.3(a) LITIGATION COSTS FOR 2017 AT THE AVERAGE

P&S Act section	Cattle (\$ millions)	Hog (\$ millions)	Poultry (\$ millions)	Total (\$ millions)
202(a) .....	2.39	0.48	4.25	7.12
202(b) .....	0.24	0.04	1.49	1.77
Total .....	2.63	0.52	5.74	8.89

TABLE 13—PROJECTED § 201.3(a) LITIGATION COSTS FOR 2017 AT THE UPPER PERCENTILE

P&S Act section	Cattle (\$ millions)	Hog (\$ millions)	Poultry (\$ millions)	Total (\$ millions)
202(a) .....	3.55	0.71	6.32	10.58
202(b) .....	0.36	0.06	2.22	2.64
Total .....	3.91	0.77	8.54	13.22

GIPSA expects § 201.3(a) to result in an additional \$4.84 million in litigation in 2017 at the lower percentile, \$8.89 million in litigation in 2017 at the average, and \$13.22 million in litigation in 2017 at the upper percentile. GIPSA also expects the majority of additional litigation to come from the poultry industry based on investigations GIPSA conducted from 2009 to 2015, many of which were based on industry complaints.

As discussed above, GIPSA considers the lower boundary of costs from § 201.3(a) to be increased litigation costs with no adjustments by the livestock and poultry industries to reduce their use of AMAs or incentive pay systems and no changes to existing marketing or production contracts. GIPSA also recognizes the uncertainty in estimating litigation costs and conducted a sensitivity analysis of litigation costs at the lower percentile, the average

percentile, and the upper percentile. The sensitivity analysis shows that litigation may vary by as much as \$8.38 million (upper percentile minus lower percentile). GIPSA believes the average litigation costs is the best available estimate of litigation costs and uses it as the lower boundary for the estimated litigation costs of § 201.3(a). The lower boundary cost estimates appear in the table below.

TABLE 14—LOWER BOUNDARY PROJECTED § 201.3(a) COSTS—PREFERRED ALTERNATIVE

P&S Act section	Cattle (\$ millions)	Hog (\$ millions)	Poultry (\$ millions)	Total (\$ millions)
202(a) .....	2.39	0.48	4.25	7.12
202(b) .....	0.24	0.04	1.49	1.77
Total .....	2.63	0.52	5.74	8.89

GIPSA estimates that § 201.3(a) will result in an additional \$8.89 million in additional litigation in the livestock and poultry industries with \$2.63 million in litigation in the cattle industry, \$0.52 million in the hog industry, and \$5.74 million in the poultry industry in the

first full year § 201.3(a) would be in place. B. Regulatory Alternative 2: Lower Boundary—Ten-Year Total Costs of the Preferred Alternative To arrive at the estimated ten-year costs of § 201.3(a), GIPSA expects the litigation costs to be constant for the

first five years while courts are setting precedents for the interpretation of § 201.3(a). GIPSA expects that case law with respect to the regulation will be settled after five years and by then, industry participants will know how GIPSA will enforce the regulation and how courts will interpret the regulation.



The effect of courts establishing precedents is that litigation costs will decline after five years as the livestock and poultry industries understand how the courts interpret the regulation.

To arrive at the estimated ten-year costs of § 201.3(a), GIPSA estimates that

litigation costs for the first five years will occur at the same rate and at the same cost as in 2017. In the second five years, GIPSA estimates that litigation costs will decrease each year and return to the baseline in the sixth year after the courts have established precedents.

GIPSA estimates this decrease in litigation costs to the baseline to be linear with the same decrease in costs each year. The total ten-year costs of § 201.3(a) at the lower boundary appears in the table below.

**TABLE 15—LOWER BOUNDARY OF TEN-YEAR TOTAL COSTS OF § 201.3(a)**

Year	Cattle (\$ millions)	Hog (\$ millions)	Poultry (\$ millions)	Total (\$ millions)
2017	2.63	0.52	5.74	8.89
2018	2.63	0.52	5.74	8.89
2019	2.63	0.52	5.74	8.89
2020	2.63	0.52	5.74	8.89
2021	2.63	0.52	5.74	8.89
2022	2.19	0.43	4.79	7.41
2023	1.75	0.35	3.83	5.93
2024	1.31	0.26	2.87	4.44
2025	0.88	0.17	1.91	2.96
2026	0.44	0.09	0.96	1.48
<b>Totals</b>	<b>19.70</b>	<b>3.90</b>	<b>43.07</b>	<b>66.67</b>

Based on the analysis, GIPSA expects the lower boundary of the ten-year total costs of § 201.3(a) to be \$66.67 million.

**C. Regulatory Alternative 2: Lower Boundary—Net Present Value of Ten-Year Total Costs of the Preferred Alternative**

The lower boundary ten-year total costs of § 201.3(a) in the table above show that the costs are constant in the first five years and then gradually decrease over the next five years. Costs to be incurred in the future are less expensive than the same costs to be incurred today. This is because the money that will be used to pay the costs in the future can be invested today and earn interest until the time period in which the cost is incurred. After the cost has been incurred, the interest earned will still be available.

To account for the time value of money, the costs of the regulation to be incurred in the future is discounted back to today's dollars using a discount rate. The sum of all costs discounted back to the present is called the net present value (NPV) of total costs. GIPSA relied on both a three percent and seven percent discount rate as discussed in Circular A-4.<sup>67</sup> GIPSA measured all costs using constant 2016 dollars.

GIPSA calculated the NPV of the ten-year total costs of the regulation using both a three percent and seven percent discount rate and the NPVs appear in the following table.

**TABLE 16—NPV OF LOWER BOUNDARY OF TEN-YEAR TOTAL COST OF § 201.3(a)—PREFERRED ALTERNATIVE**

Discount rate	Preferred alternative (\$ millions)
3 Percent	58.62
7 Percent	50.03

GIPSA expects the NPV of the lower boundary of the ten-year total costs of § 201.3(a) to be \$58.62 million at a three percent discount rate and \$50.03 million at a seven percent discount rate.

**D. Regulatory Alternative 2: Lower Boundary—Annualized NPV of Ten-Year Total Costs of the Preferred Alternative**

GIPSA then annualized the NPV of the ten-year total costs (referred to as annualized costs) of § 201.3(a) at the lower boundary using both a three percent and seven percent discount rate as required by Circular A-4 and the results appear in the following table.<sup>68</sup>

**TABLE 17—ANNUALIZED COSTS OF § 201.3(a)—PREFERRED OPTION**

Discount rate	Preferred alternative (\$ millions)
3 Percent	6.87
7 Percent	7.12

GIPSA expects the annualized costs of § 201.3(a) at the lower boundary to be

\$6.87 million at a three percent discount rate and \$7.12 million at a seven percent discount rate.

**E. Regulatory Alternative 2: Upper Boundary of Cost Spectrum—Preferred Alternative**

As discussed above, the upper boundary of the cost spectrum occurs if the cattle, hog, and poultry industries adjust their use of AMAs and incentive pay systems and make systematic changes in their marketing and production contracts to reduce the threat of litigation. For the upper boundary cost estimate, GIPSA relied on the Informa Study and Elam Study. The Informa Study was prepared for the NMA and the Elam Study was prepared for the NCC. Both of these groups were opposed to the rule proposed on June 22, 2010 and GIPSA considers their studies to be upper boundary scenarios for meat and livestock industries and poultry industry costs.

GIPSA reviewed the Informa Study and the Elam Study and compared the provisions in the multiple proposed regulations in the June 22, 2010 rule against § 201.3(a). The Informa Study estimated both direct and indirect costs of the 2010 proposed rule. The Informa Study direct costs are estimates of actual costs of complying with all of the regulations proposed in 2010, such as new computer software and additional staff. The Informa Study estimated both direct one-time costs and on-going direct costs that would be incurred by the livestock industry each year. The Informa Study also estimated indirect costs to capture livestock and poultry industry adjustments to the 2010

<sup>67</sup> [https://www.whitehouse.gov/sites/default/files/omb/assets/regulatory\\_matters\\_pdf/a-4.pdf](https://www.whitehouse.gov/sites/default/files/omb/assets/regulatory_matters_pdf/a-4.pdf). Accessed on September 19, 2016.

<sup>68</sup> Ibid.

regulations. The Informa Study also included litigation costs.

The sources of indirect costs that the Informa Study estimated for the cattle industry are a reduction in production efficiencies due to a reduction in the use of AMAs and the corresponding reduction in premiums paid in branded beef programs and a reduction in beef quality. The RTI Study also found that hypothetical reductions in AMAs would reduce beef and cattle supplies, reduce the quality of beef, and increase retail and wholesale beef prices.<sup>69</sup>

For the hog industry, the Informa Study estimated the indirect costs as the reduction in operational efficiency from operating slaughter plants at less than full optimal utilization as well as

revenue losses due to reductions in quality from reductions in premiums paid for higher quality hogs procured under AMAs.

For the poultry industry, the Informa Study estimated indirect costs resulting from a slowdown in the adoption of new technology that increases efficiency as integrators are unwilling to provide monetary incentives for growers to invest in new technology due to the threat of litigation for unfair, unjustly discriminatory, or deceptive payment practices.

The Informa Study recognized that the economic costs of the 2010 rule would take time to materialize. The Informa Study estimated that only the direct, one-time costs would occur

shortly after implementation of the regulations in the 2010 rule and the more significant impacts, such as declining efficiency and quality degradation, would happen more slowly and might not reach the full impact until three or four years after the rule became effective.<sup>70</sup> The Informa Study further recognized that companies would find ways to adapt to the provisions of the regulation in the rule and the impact of the rule would be lessened over time.<sup>71</sup> The following table summarizes the full-impact of the Informa Study cost estimates on the impact of the June 22, 2010 proposed rule.

TABLE 18—TOTAL INFORMA STUDY COSTS FOR THE FULL-IMPACT YEAR<sup>72</sup>

	Cattle (\$ millions)	Hogs (\$ millions)	Poultry (\$ millions)	Total (\$ millions)
One-Time Direct Costs .....	38.7	68.7	26.0	133.4
Ongoing Direct Costs .....	61.5	73.8	33.4	168.7
Cost Increase Due to Efficiency Loss .....	401.9	176.7	302.2	880.8
Revenue Lost Due to Quality/Demand Impact .....	377.7	82.2	0.0	459.9
<b>Total Informa Costs .....</b>	<b>879.8</b>	<b>401.4</b>	<b>361.6</b>	<b>1,642.8</b>

At the full impact level, the Informa Study estimated the highest cost to be borne by the cattle industry at almost \$880 million, followed by the hog and poultry industries. The Informa Study estimated that the total costs of the regulations proposed in 2010 could be as high as \$1.64 billion and that this cost would not be fully borne until three or four years after implementation of the regulations.

The Elam Study estimated a similar impact on the poultry industry as the Informa Study. The Elam Study estimated that the costs of the 2010 proposed rule would increase over time and would cost the chicken industry \$200.64 million in the third year after implementation, \$266.94 in the fourth year, and \$336.67 million in the fifth year, with a total cost of \$1.03 billion over the first five years.<sup>73</sup> The Elam Study estimated \$6 million as one-time administrative costs from re-drafting poultry grower contracts, additional record keeping, and submission of contracts to GIPSA.<sup>74</sup> The remainder of the costs estimated in the Elam Study were indirect costs resulting from

efficiency losses and costs of testing and evaluating feed.

GIPSA expects the livestock and poultry industries to adapt to § 201.3(a) after a period of five years when the courts have presumably settled the case law and the livestock and poultry industries know how courts will interpret the regulation. This will cause the costs of § 201.3(a) to decline after a period of five years. GIPSA expects the livestock and poultry industries to adjust their business practices in a way to maximize profits and lessen the impact of the regulation over time.

GIPSA also compared the estimated impact on the poultry industry in the first five years as estimated in the Informa Study and the Elam Study. In the first four years, the poultry costs estimated in the Informa Study are higher than those estimated in the Elam Study. The Elam study has higher cost estimates in year five. Because the Informa Study cost estimates are higher than the Elam Study cost estimates and the Informa Study cost estimates decline in the later years as GIPSA expects, GIPSA relies on the Informa Study cost

estimates to estimate the upper boundary of the costs of § 201.3(a).

1. Regulatory Alternative 2: Upper Boundary-Informa Study Estimates—Adjustment 1

In order to arrive at the upper boundary estimate of the costs of § 201.3(a), GIPSA made several downward adjustments to the Informa Study estimates presented in Table 18 above. The first adjustment is to reduce the Informa Study cost estimates by 25 percent. The Informa Study implicitly asserted that 75 percent of the total costs of the 2010 rule were caused by relieving the plaintiff of the burden of proving competitive injury.<sup>75</sup> Thus, the Informa Study implicitly asserted that provisions in regulations in the 2010 proposed rule other than § 201.3(a) are responsible for 25 percent of the total costs. Because GIPSA is only concerned with costs attributable to § 201.3(a), GIPSA is reducing the Informa Study cost estimates by 25 percent.

<sup>69</sup> RTI International, 2007, GIPSA Livestock and Meat Marketing Study. Prepared for Grain Inspection, Packers and Stockyard Administration.

<sup>70</sup> Informa Economics, Inc. “An Estimate of the Economic Impact of GIPSA’s Proposed Rules,” prepared for the National Meat Association, 2010, Page 66.

<sup>71</sup> Ibid, Page 67.

<sup>72</sup> Ibid, Tables 7, 8, and 9.

<sup>73</sup> Elam, Dr. Thomas E. “Proposed GIPSA Rules Relating to the Chicken Industry: Economic Impact.” FarmEcon LLC, 2010, Table on Page 25.

<sup>74</sup> Ibid, Page 21.

<sup>75</sup> Informa Economics, Inc. “An Estimate of the Economic Impact of GIPSA’s Proposed Rules,” prepared for the National Meat Association, 2010, Page 71.

2. Regulatory Alternative 2: Upper Boundary-Informa Study Estimates—Adjustment 2

The second downward adjustment that GIPSA made is to scale the Informa

Study’s estimates according to the timing of the economic impact the Informa Study estimated. The Informa Study expected the costs to increase in the first three years, peak in years three or four, and then decline through year

ten. In order to simulate the costs that the Informa Study assigned to each year, GIPSA adjusted the costs in the full impact year in Table 18 above by the percentages listed in Table 19.

TABLE 19—IMPACT LEVEL OF INFORMA STUDY COSTS <sup>76</sup>

Year	Cattle (%)	Hog (%)	Poultry (%)
2017	40	29	49
2018	69	59	79
2019	100	79	100
2020	100	100	100
2021	100	96	81
2022	91	75	60
2023	75	54	30
2024	51	53	9
2025	38	29	9
2026	38	29	9

GIPSA then weighted the Informa Study’s full-impact cost estimate for each year and each industry by the impact level from the table above.

3. Regulatory Alternative 2: Upper Boundary-Informa Study Estimates—Adjustment 3

The final downward adjustment GIPSA made is based on two factors. The first factor is that GIPSA expects the language in § 201.3(a) to result in limited industry adjustments and a continued role for the courts to interpret when a showing of harm or likelihood of harm to competition is necessary in order to prove a violation of section 202(a) or (b) of the P&S Act. The second factor is the fact that the courts have historically not required a showing of harm or likelihood of harm to competition in all livestock and poultry cases and GIPSA expects that trend to continue. GIPSA discusses the factors in turn and then estimates the third and final adjustment to the Informa Study estimates.

The first factor is that § 201.3(a) states that a finding that the challenged conduct or action adversely affects or is likely to adversely affect competition is not necessary in all cases. However, § 201.3(a) does not provide any guidance regarding the types of conduct or action where a finding of harm or likelihood of harm would or would not be necessary to prove a violation of

section 202(a) or (b) of the P&S Act.<sup>77</sup> It is possible that without the guidance in the proposed regulations, courts will continue to exercise judicial discretion in determining when a finding of harm or likelihood of harm to competition is necessary in order to prove a violation of sections 202(a) and/or (b). However, this rule will provide the longstanding position of the Department of Agriculture for the courts to consider. Because some of the U.S. Courts of Appeals in areas of heavy agricultural production have ruled that GIPSA must demonstrate competitive injury or the likelihood of competitive injury in order to prove that certain conduct or action violates section 202(a) and (b), GIPSA anticipates that the federal district courts in those circuits will continue to apply this binding case law.

GIPSA acknowledges that final § 201.3(a) may motivate some private plaintiffs to file new lawsuits under sections 202(a) and/or 202(b) to test its parameters in an attempt to move courts to find in selected cases that harm or likely harm to competition need not be proven. If a U.S. Court of Appeals upholds a district court ruling that competitive harm or likelihood of competitive harm must be demonstrated in order to prove a violation of section 202(a) or (b), that result would not involve any change from the status quo of section 202(a) and 202(b) litigation. Packers, swine contractors, and live

poultry dealers would have no reason to adjust their contracts or business practices with the result of few additional indirect costs being borne by the livestock and poultry industries. Similarly, plaintiffs would then need to consider the high costs (in terms of discovery of large amounts of data and the hiring of economic and statistical experts) to proceed to trial and may opt not to proceed with additional litigation.<sup>78</sup>

GIPSA expects the effects of § 201.3(a) on livestock and poultry industry participants to be mixed. A small number of livestock producers, swine production contract growers, and poultry growers may seek judicial enforcement of their rights under the P&S Act without showing harm or likely harm to competition. However, due to the uncertain outcome of litigation under sections 202(a) and/or 202 (b), GIPSA expects packers, swine contractors, and live poultry dealers will likely take a “wait and see” approach prior to making any significant changes in their business models, marketing arrangements, or other practices. Concerned with net profit and reports to stockholders or owners, such firms will rationally forego any large changes in their operations until it is clear that such changes are legally required. If such changes are not required, due to status quo rulings by courts requiring proof of competitive

<sup>76</sup> The Informa Study estimates are for years one through ten beginning with the first year of the implementation of the rule and are not specific to any one year. GIPSA uses 2017 as year one and 2026 as year ten. The Informa Study stated that in particular, the decline in beef and pork quality and subsequent damage to consumer demand will take time to materialize, while the efficiency losses in poultry would likely happen sooner, but will still

be delayed. This is presumably because the breeding cycle for hogs and especially for cattle is longer than that for poultry.

<sup>77</sup> Proposed regulations 201.210 and 201.211 provide conduct and criteria for 202(a) and 202(b) violations.

<sup>78</sup> In the *Been v. O.K. Indus., Inc.* litigation, the plaintiffs’ economic expert billed for more than

3,000 hours spent on economic analysis of data, building a monopsony case in accordance with the Tenth Circuit’s 2007 opinion, writing reports, consulting with attorneys, and testifying at depositions and during the jury trial. The defendant’s two economic experts presumably billed for a similarly significant amount of time.

injury or the likelihood of competitive injury, as GIPSA anticipates, then GIPSA expects that few changes will be made as a result of § 201.3(a).

GIPSA expects the status quo enforcement outcome of § 201.3(a) discussed above to be most likely in the cattle and hog industries. GIPSA has enforced the P&S Act and regulations against packers without proving harm or likelihood of harm to competition for decades, and the courts have upheld successful enforcement actions. It is primarily in the poultry industry that, the courts have declined to enforce, sections 202(a) and (b) of the P&S Act and regulations without a finding of harm or likelihood of harm to competition.

Therefore, due to the likelihood of status quo rulings, GIPSA estimates that the upper boundary cost estimate of the overall impact of § 201.3(a) on the cattle and hog industries will be considerably less than the Informa Study estimates after applying the first two adjustments.

The second factor is the recent outcome of cases decided under the P&S Act since 2000 and whether courts have required demonstration of harm or likely harm to competition. GIPSA examined the actual number of cases decided under the P&S Act from 2000 to 2014. This is the same listing of cases as in the estimation of litigation costs presented earlier, except that GIPSA only considered cases decided after 2000 to reflect the most current decisions reached by the courts. The listing of court decisions and the court in which the decision was reached came from the National Agricultural Law Center at the University of Arkansas.<sup>79</sup> GIPSA then reviewed each case since

2000 and classified it as either a competition, financial, or trade practice case. GIPSA then examined each case to determine which cases involved alleged violations of sections 202(a) and 202(b) and which of those cases the court required demonstration of harm or likelihood of harm to competition.

GIPSA found 22 cases which involved alleged violations of sections 202(a) and 202(b) and addressed the issue of demonstrating harm or likelihood of harm to competition. Of those 22 cases, GIPSA found that the courts required demonstration of harm or likelihood of harm to competition in eight cases and did not require demonstration of a harm or likelihood of harm to competition in 14 cases. However, these 14 cases where demonstration of harm or likelihood of harm to competition was not required were not evenly distributed among the cattle, hog, and poultry industries. Courts have only required a demonstration of harm or likelihood of harm to competition in 20 percent of the cases alleging violations of sections 202(a) and 202(b) in the cattle and hog industries since 2000. GIPSA found that the courts have required a demonstration of harm or likelihood of harm to competition in 50 percent of the cases alleging violations of sections 202(a) and 202(b) in the poultry industry since 2000. The fact that demonstration of harm or likelihood of harm to competition was not required in every case is consistent with § 201.3(a), which states that demonstration of harm or likelihood of harm to competition is not required in all cases. As these cases have all involved livestock packers, swine contractors, and live poultry

dealers and are a matter of public record, GIPSA believes that packers, swine contractors, and live poultry dealers are already aware that courts have not required demonstration of a harm or likelihood of harm to competition in all cases. This is another reason why GIPSA expects packers, swine contractors, and live poultry dealers to likely take a “wait and see” approach.

Therefore, due to the likelihood of status quo rulings by courts and the rationality of livestock packers, swine contractors, and live poultry dealers to tend toward a “wait and see” approach, GIPSA estimates the upper boundary estimate to be between 20 percent of the Informa Study cattle and hog industry estimates, 50 percent of the Informa Study poultry industry estimate and zero percent of the Informa Study estimates after applying the first two adjustments. Zero percent would mean that there are no industry adjustments from § 201.3(a).

Given the uncertainty in how the industry will respond to § 201.3(a), GIPSA selected one half of 20 percent of the Informa Study estimates for cattle and hogs, one half of 50 percent of the poultry industry estimate from the Informa Study estimates as its point estimate. Thus, GIPSA applied ten percent of the cattle and hog Informa Study estimates and 25 percent of the poultry Informa Study estimates as its point estimate after applying the first two adjustments. The following table shows the estimated upper boundary costs for § 201.3(a) on an annual and ten-year cost basis based on the adjusted Informa Study cost estimates.

TABLE 20—UPPER BOUNDARY ANNUAL COSTS OF § 201.3(a)—PREFERRED ALTERNATIVE

Year	Cattle (\$ millions)	Hog (\$ millions)	Poultry (\$ millions)	Total (\$ millions)
2017	28.14	12.49	35.87	76.49
2018	43.67	14.68	49.78	108.13
2019	63.08	19.82	62.93	145.82
2020	63.08	24.95	62.93	150.96
2021	63.08	23.85	50.72	137.65
2022	57.26	18.71	37.57	113.54
2023	47.55	13.58	18.78	79.92
2024	32.03	13.21	5.64	50.87
2025	24.26	7.34	5.64	37.24
2026	24.26	7.34	5.64	37.24
Totals	446.42	155.97	335.47	937.86

At the upper boundary in the first full year after implementation, GIPSA estimates that § 201.3(a) will result in an

additional \$76.49 million in direct and indirect costs in the livestock and poultry industries, with \$28.14 million

in the cattle industry, \$12.49 million in the hog industry, and \$35.87 million in the poultry industry. GIPSA expects the

<sup>79</sup> <http://nationalaglawcenter.org/aglaw-reporter/case-law-index/packers-and-stockyards>.

upper boundary of the ten-year total cost of § 201.3(a) to be \$937.86 million.

**F. Regulatory Alternative 2: Upper Boundary—NPV of Ten-Year Total Costs of the Preferred Alternative**

GIPSA calculated the NPV of the ten-year total costs of the regulation using both a three percent and seven percent discount rate and the NPVs appear in the following table.

**TABLE 21—NPV OF UPPER BOUNDARY OF TEN-YEAR TOTAL COST OF § 201.3(a)—PREFERRED ALTERNATIVE**

Discount rate	Preferred option (\$ millions)
3 Percent .....	818.97
7 Percent .....	692.49

GIPSA expects the NPV of the upper boundary of the ten-year total costs of § 201.3(a) to be \$818.97 million at a three percent discount rate and \$692.49 million at a seven percent discount rate.

**G. Regulatory Alternative 2: Upper Boundary—Annualized Costs of the Preferred Alternative**

GIPSA then annualized the costs of § 201.3(a) at the upper boundary using

both a three percent and seven percent discount rate and the results appear in the following table.

**TABLE 22—ANNUALIZED COSTS OF § 201.3(a)—PREFERRED OPTION**

Discount rate	Preferred option (\$ millions)
3 Percent .....	96.01
7 Percent .....	98.60

GIPSA expects the annualized costs of § 201.3(a) at the upper boundary to be \$96.01 million at a three percent discount rate and \$98.60 million at a seven percent discount rate.

**H. Sensitivity Analysis of the Upper Boundary**

In the section above, GIPSA explained that it chose 10 percent of the cattle and hog estimates from the Informa Study and 25 percent of the poultry estimate from the Informa Study as its point estimate for the upper boundary costs. Because of the uncertainty over the eventual impacts of this rule on industry behavior, GIPSA evaluates the sensitivity of its upper bound estimate to an alternative set of assumptions. GIPSA presents three alternative sets of

assumptions for calculating the upper bound estimate.

For the first scenario, GIPSA applies the full adjustment to the Informa Study cost estimates, specifically, 20 percent for cattle and hogs and 50 percent for poultry. In that case, GIPSA's estimate of the upper bound would be twice as high as presented in the previous section. For the second scenario, § 201.3(a) is assumed to impact industry behavior for the poultry industry only, (that is, zero percent of the Informa Study estimate for cattle and hogs, and 25 percent of the estimate for poultry). In that scenario, the upper bound estimate would be the same as presented in Table 20, above, for poultry, and would be the lower boundary estimate for cattle and hogs as shown in Table 15. For a third scenario, all the Informa Study estimates are adjusted to zero assuming that there are no indirect costs of adjustment to the rule. In that case, the lower boundary estimate, only reflecting litigation costs, as shown in Tables 15 through 17 would be the result.

GIPSA calculated the NPV of the ten-year total costs of the regulation using both a three percent and seven percent discount rate for each of the three scenarios described above and the NPVs appear in the following table.

**TABLE 23—SENSITIVITY ANALYSIS OF THE UPPER BOUNDARY ESTIMATE OF THE TEN-YEAR TOTAL COST OF § 201.3(a)—PREFERRED ALTERNATIVE—EXPRESSED IN NPV**

Discount rate	Point estimate (\$ millions)	Scenario 1 (\$ millions)	Scenario 2 (\$ millions)	Scenario 3 (\$ millions)
3 Percent .....	818.97	1,637.94	319.43	58.62
7 Percent .....	692.49	1,384.98	276.18	50.03

Scenario 1: Adjustment to Informa of 20% for cattle and hogs, 50% for poultry.  
 Scenario 2: Adjustment to Informa of 0% for cattle and hogs, 25% for poultry.  
 Scenario 3: Adjustment to Informa of 0% for cattle and hogs, and poultry.

GIPSA then annualized the estimated costs of § 201.3(a) at the upper boundary

for the three sensitivity scenarios using both a three percent and seven percent

discount rate and the results appear in the following table.

**TABLE 24—SENSITIVITY ANALYSIS OF THE UPPER BOUNDARY ESTIMATE OF THE TEN-YEAR TOTAL COST OF § 201.3(a)—PREFERRED ALTERNATIVE—ANNUALIZED**

Discount rate	Point estimate (\$ millions)	Scenario 1 (\$ millions)	Scenario 2 (\$ millions)	Scenario 3 (\$ millions)
3 Percent .....	96.01	192.02	37.45	6.87
7 Percent .....	98.60	197.19	39.32	7.12

Scenario 1: Adjustment to Informa of 20% for cattle and hogs, 50% for poultry.  
 Scenario 2: Adjustment to Informa of 0% for cattle and hogs, 25% for poultry.  
 Scenario 3: Adjustment to Informa of 0% for cattle and hogs, and poultry.

**I. Regulatory Alternative 2: Range of Annualized Costs of the Preferred Alternative**

The following table shows the full range of the annualized costs of

§ 201.3(a) at both a three percent and seven percent discount rate.

TABLE 25—RANGE OF ANNUALIZED COSTS—PREFERRED OPTION

Discount rate	Lower boundary (\$ millions)	Upper boundary (\$ millions)
3 Percent .....	6.87	96.01
7 Percent .....	7.12	98.60

GIPSA estimates the annualized costs of § 201.3(a) will range from \$6.87 million to \$96.01 million at a three percent discount rate and from \$7.12 million to \$98.60 million at a seven percent discount rate.

*J. Regulatory Alternative 2: Point Estimate of Annualized Costs of the Preferred Alternative*

The range of potential costs is broad. The reason there is a broad range of

potential costs is because § 201.3(a) has applicability to the livestock and poultry industries and it is difficult to predict how the industries will respond. If the industries do not change any of their current business practices, GIPSA expects additional litigation to be the only costs and the costs of the regulation will be closer to the lower boundary. If, however, the industries respond by reducing the use of AMAs

and restricting their use of incentive pay, GIPSA expects the costs of the regulation to be closer to the upper boundary. Based on the uncertainty over how the industries will respond, GIPSA believes that the mid-point in the range of estimated annualized costs is the best available point estimate of the costs of § 201.3(a). The point estimate along with the lower and upper boundary estimates appear in the table below.

TABLE 26—POINT ESTIMATE OF ANNUALIZED COSTS—PREFERRED ALTERNATIVE

Discount rate	Lower boundary (\$ millions)	Point estimate (\$ millions)	Upper boundary (\$ millions)
3 Percent .....	6.87	51.44	96.01
7 Percent .....	7.12	52.86	98.60

GIPSA expects the annualized costs of § 201.3(a) at the point estimate to be \$51.44 million at a three percent discount rate and \$52.86 million at a seven percent discount rate. Based on the discussion of GIPSA’s expectation that the cattle, hog, and poultry industries will likely take a “wait and see” approach to how the courts will interpret § 201.3(a) and for courts to take a status quo approach, GIPSA believes the point estimates of the preferred

alternative to be the best available estimates of the costs of § 201.3(a).

*K. Regulatory Alternative 2: Sensitivity Analysis of Point Estimates of Annualized Costs*

In its estimate of litigation costs presented above, GIPSA recognized the uncertainty in estimating litigation costs and conducted a sensitivity analysis. GIPSA estimated that the lower boundary of the first-year costs of § 201.3(a) were \$4.84 million at the

lower percentile, \$8.89 million at the average percentile, and \$13.22 million at the upper percentile.<sup>80</sup> GIPSA relied on the average estimate of litigation costs as the lower boundary of the litigation costs of § 201.3(a).

To consider the effects of the uncertainty in its estimation of litigation costs, GIPSA annualized its litigation costs estimates at the lower percentile, the average percentile, and the upper percentile and the results appear in the following table.

TABLE 27—ANNUALIZED RANGE OF ESTIMATED LITIGATION COSTS—PREFERRED ALTERNATIVE

Discount rate	Lower percentile (\$ millions)	Average (\$ millions)	Upper percentile (\$ millions)
3 Percent .....	3.74	6.87	10.22
7 Percent .....	4.54	7.12	12.41

GIPSA then applied this uncertainty to its point estimates of the annualized costs of § 201.3(a) by subtracting the difference of the lower percentile of estimated litigation costs and the point

estimate at both the three and seven percent discount rates and added the difference of the upper percentile of estimated litigation costs and the point estimate at both the three and seven

percent discount rates. The results of the sensitivity analysis appear in the following table.

<sup>80</sup> See Tables 11–13 above.

TABLE 28—ANNUALIZED RANGE OF POINT ESTIMATES OF § 201.3(a)—PREFERRED ALTERNATIVE

Discount rate	Lower percentile (\$ millions)	Point estimate (\$ millions)	Upper percentile (\$ millions)
3 Percent .....	49.87	51.44	53.11
7 Percent .....	51.57	52.86	55.50

GIPSA estimates that the point estimates of the annualized costs of § 201.3(a) will range from \$49.87 million at the lower percentile to \$53.11 million at the upper percentile using a three percent discount rate. At the seven percent discount rate, GIPSA estimates that the point estimate of the annualized costs will range from \$51.57 million at the lower percentile to \$55.50 million at the upper percentile. Given the size of the range between the upper and lower boundary of the estimated annualized costs, GIPSA's point estimate is not overly sensitive to the uncertainty in the estimated litigation costs. Thus, GIPSA believes the point estimates of the preferred alternative to be the best available estimate of the costs of § 201.3(a).

*L. Regulatory Alternative 2: Benefits of the Preferred Alternative*

GIPSA was unable to quantify the benefits of § 201.3(a). However, there are qualitative benefits of § 201.3(a) that merit discussion. The primary qualitative benefit of § 201.3(a) is ability of livestock producers, swine production contract growers, and poultry growers to have more protections and be treated more fairly, which may lead to more equitable contracts. A simple example is the inaccurate weighing of slaughter-ready poultry grown by a poultry grower for a live poultry dealer. The poultry grower is harmed if the true weight is above the inaccurate weight because the poultry grower's payment is typically tied to the poultry grower's efficiency in growing poultry, which in this case is artificially low due to the inaccurate weight of the live birds. The impact of this harm to the poultry grower is very small when compared to the entire industry and there is no discernible or provable harm to competition from this one instance. However because there is no discernible or provable harm or likely harm to competition, courts have been reluctant to find a violation of section 202(a) of the P&S Act in such a situation, despite the harm suffered by the individual poultry grower.

However, if similar, though unrelated, harm is experienced by a large number of poultry growers, the cumulative effect does result in a discernible and provable

harm to competition. The individual harm is inconsequential to the poultry industry, but the sum total of all individual harm has the potential to be quite significant when compared to the poultry industry and therefore, courts have found harm or likely harm to competition in such a situation. Under proposed § 201.210(b)(8), failing to ensure accurate weights of live poultry, absent a legitimate business justification, will constitute an unfair, unjustly discriminatory, or deceptive practice or device and a violation of section 202(a) of the P&S Act. Whether or not the conduct harms or is likely to harm competition becomes irrelevant.

GIPSA expects § 201.3(a) to increase enforcement actions against live poultry dealers for violations of sections 202(a) and/or 202(b) when the conduct or action does not harm or is not likely to harm competition. Several appellate courts have disagreed with USDA's interpretation of the P&S Act that harm or likely harm to competition is not necessary in all cases to prove a violation of sections 202(a) and/or 202(b). In some cases in which the United States was not a party, these courts have concluded that plaintiffs could not prove their claims under sections 202(a) and/or (b) without proving harm to competition or likely harm to competition. One reason the courts gave for declining to defer to USDA's interpretation of the statute is that USDA had not previously enshrined its interpretation in a regulation. Interim final § 201.3(a) corrects the issue and courts may now give deference to USDA's interpretation.

GIPSA expects the result will be additional enforcement actions that will be successfully litigated and serve as a deterrent to violating sections 202(a) and/or 202(b). Benefits to the industries and the markets from additional enforcement will also arise from establishing parity of negotiating power between livestock producers, swine production contract growers, and poultry growers and packers, swine contractors, and live poultry dealers by reducing the ability to use market power with the resulting dead weight losses.<sup>81</sup>

<sup>81</sup> Nigel Key and Jim M. MacDonald discuss evidence for the effect of concentration on grower

Section 201.3(a) also provides additional protections for livestock producers, swine production contract growers, and poultry growers against unfair, unjustly discriminatory, and deceptive practices or devices and undue or unreasonable preferences, advantages, prejudices, or disadvantages since demonstration of harm to competition is required in all cases. GIPSA believes the standard articulated in § 201.3(a) is consistent with its mission "[T]o protect fair trade practices, financial integrity, and competitive markets for livestock, meats, and poultry."<sup>82</sup> By making it clear that demonstration of harm or likely harm to competition is not necessary in all cases, this interim final rule promotes fairness and equity for livestock producers, swine production contract growers, and poultry growers.<sup>83</sup>

*M. Regulatory Alternative 2: Cost-Benefit Summary of the Preferred Alternative*

GIPSA estimates the annualized costs of § 201.3(a) to range from \$6.87 million to \$96.01 million at the three percent discount rate and from \$7.12 million to \$98.60 million at the seven percent discount rate. The range of potential costs is broad. GIPSA relied on its expertise to arrive at a point estimate range of expected annualized costs. GIPSA expects that the cattle, hog, and poultry industries will primarily take a "wait and see" approach to how courts will interpret § 201.3(a) and courts to take a status quo approach and only slightly adjust their use of AMAs and performance-based payment systems. GIPSA estimates that the annualized costs of § 201.3(a) will be \$51.44 million at a three percent discount rate and \$52.86 million at a seven percent discount rate based on an anticipated "wait and see" approach and industry adjustments.

compensation in "Local Monopsony Power in the Market for Broilers? Evidence from a Farm Survey" selected paper American Agri. Economics Assn. meeting Orlando, FL, July 27–29, 2008.

<sup>82</sup> [https://www.gipsa.usda.gov/laws/law/PS\\_act.pdf](https://www.gipsa.usda.gov/laws/law/PS_act.pdf). Accessed on September 19, 2016.

<sup>83</sup> See additional discussion in Steven Y. Wu and James MacDonald (2015) "Economics of Agricultural Contract Grower Protection Legislation," *Choices* 30(3): 1–6.



The primary benefit of § 201.3(a) is the increased ability for the enforcement of the P&S Act for violations of sections 202(a) and/or 202(b), which do not result in harm or likely harm to competition. This, in turn, will reduce instances of unfair, unjustly discriminatory, or deceptive practices or devices and undue or unreasonable preferences, advantages, prejudices, or disadvantages and increased efficiencies in the marketplace. The benefit of additional enforcement of the P&S Act will accrue to all segments of the value chain in the production of livestock and poultry, and ultimately to consumers.

**N. Regulatory Alternative 3: Small Business Exemption**

The third regulatory alternative that GIPSA considered is issuing § 201.3(a) as an interim final regulation, but exempting small businesses, as defined by the Small Business Administration, from having to comply with it.<sup>84</sup> To

estimate the expected costs of exempting small business, GIPSA relied on the percentage of small businesses in the cattle, hog, and poultry industries that are developed and presented in the Regulatory Flexibility Analysis section below.

To arrive at the estimated costs of § 201.3(a) based on exempting small businesses, GIPSA weighted the point estimates, lower boundary, and upper boundary of cost estimates by the percentage of cattle and hogs processed by packers that are large businesses and the percentage of contracts held by swine contractors and live poultry dealers that are large businesses. GIPSA estimates that small businesses account for 19.3 percent of the cattle slaughtered. For the hog industry, GIPSA estimates that small businesses slaughter 17.8 percent of hogs and that 65 percent of swine contractors are small businesses. GIPSA estimates that

10.27 percent of live poultry dealers are classified as small businesses.

**O. Regulatory Alternative 3: Lower Boundary of Cost Spectrum—Litigation Costs of the Small Business Exemption**

As discussed above, GIPSA considers the lower boundary of costs from § 201.3(a) to be increased litigation with no adjustments by the cattle, hog, and poultry industries to reduce their use of AMAs or incentive pay systems and there are no changes to existing marketing or production contracts. GIPSA used the average of the litigation cost estimates as the lower boundary for the estimated costs of § 201.3(a). GIPSA then weighted the lower boundary cost estimate under the preferred alternative by the percentage of large businesses in the cattle, hog, and poultry industries. The estimates appear in the table below. The preferred alternative is also shown for convenience.

**TABLE 29—LOWER BOUNDARY ANNUAL TOTAL COSTS—SMALL BUSINESS EXEMPTION**

Year	Preferred alternative (\$ millions)	Small business exemption (\$ millions)
2017	8.89	7.49
2018	8.89	7.49
2019	8.89	7.49
2020	8.89	7.49
2021	8.89	7.49
2022	7.41	6.24
2023	5.93	4.99
2024	4.44	3.74
2025	2.96	2.50
2026	1.48	1.25
<b>Totals</b>	<b>66.67</b>	<b>56.16</b>

At the lower boundary with a small business exemption, GIPSA estimates that § 201.3(a) will result in an additional \$7.49 million in litigation costs in the cattle, hog, and poultry industries in the first full year following implementation. GIPSA expects the lower boundary of the ten-year total

costs of § 201.3(a) with a small business exemption to be \$56.16 million.

**P. Regulatory Alternative 3: Lower Boundary—NPV of Total Costs of the Small Business Exemption**

GIPSA calculated the lower boundary of the NPV of the ten-year total costs of

the regulation under the small business exemption using both a three percent and seven percent discount and the NPVs appear in the following table. The preferred alternative is also shown for convenience.

**TABLE 30—LOWER BOUNDARY NPV OF TEN-YEAR TOTAL COST—SMALL BUSINESS EXEMPTION**

Discount rate	Preferred alternative (\$ millions)	Small business exemption (\$ millions)
3 Percent	58.62	49.38
7 Percent	50.03	42.14

<sup>84</sup> See: [http://www.sba.gov/idc/groups/public/documents/sba\\_homepage/serv\\_sstd\\_tablepdf.pdf](http://www.sba.gov/idc/groups/public/documents/sba_homepage/serv_sstd_tablepdf.pdf).

GIPSA expects the NPV of the lower boundary of the ten-year total costs of § 201.3(a) under a small business exemption to be \$49.38 million at a three percent discount rate and \$42.14 million at a seven percent discount rate.

Q. Regulatory Alternative 3: Lower Boundary—Annualized Costs of the Small Business Exemption

GIPSA then annualized the NPV of the ten-year total costs of § 201.3(a) at

the lower boundary using both a three percent and seven percent discount rate and the results appear in the following table. The preferred alternative is also shown for convenience.

TABLE 31—LOWER BOUNDARY OF ANNUALIZED COSTS—SMALL BUSINESS EXEMPTION

Discount rate	Preferred alternative (\$ millions)	Small business exemption (\$ millions)
3 Percent	6.87	5.79
7 Percent	7.12	6.00

GIPSA expects the annualized costs of § 201.3(a) at the lower boundary with a small business exemption to be \$5.79 million at a three percent discount rate and \$6.00 million at a seven percent discount rate.

R. Regulatory Alternative 3: Upper Boundary of Cost Spectrum—Small Business Exemption

As discussed above, the upper boundary of the cost spectrum occurs if

the cattle, hog, and poultry industries adjust their use of AMAs and incentive pay systems and make systematic changes in their marketing and production contracts to reduce the threat of litigation.

For the upper boundary cost estimates under the small business exemption, GIPSA weighted the upper boundary cost estimates under the preferred alternative by the percentage of large

businesses in the cattle, hog, and poultry industries and the estimates appear in the table below. For convenience, the estimated costs of the preferred alternative are shown in addition to the costs of the small business exemption.

TABLE 32—UPPER BOUNDARY ANNUAL TOTAL COSTS—SMALL BUSINESS EXEMPTION

Year	Preferred alternative (\$ millions)	Small business exemption (\$ millions)
2017	76.49	60.08
2018	108.13	86.00
2019	145.82	115.60
2020	150.96	117.73
2021	137.65	106.32
2022	113.54	87.69
2023	79.92	60.87
2024	50.87	36.39
2025	37.24	27.68
2026	37.24	27.68
Totals	937.86	726.05

At the upper boundary with a small business exemption, GIPSA estimates that § 201.3(a) will result in an additional \$60.08 million in direct and indirect costs in the cattle, hog, and poultry industries in the first full year following implementation. GIPSA expects the upper boundary of the ten-

year total costs of § 201.3(a) with a small business exemption to be \$726.05 million.

S. Regulatory Alternative 3: Upper Boundary—NPV of Ten-Year Total Costs of the Small Business Exemption

GIPSA calculated the upper boundary of the NPV of the ten-year total costs of

the regulation under the small business exemption using both a three percent and seven percent discount and the NPVs appear in the following table. The preferred alternative is also shown for convenience.

TABLE 33—UPPER BOUNDARY NPV OF TEN-YEAR TOTAL COSTS—SMALL BUSINESS EXEMPTION

Discount rate	Preferred alternative (\$ millions)	Small business exemption (\$ millions)
3 Percent	818.97	634.97
7 Percent	692.49	537.90

GIPSA expects the NPV of the upper boundary of the NPV of the ten-year total costs of § 201.3(a) under a small business exemption to be \$634.97 million at a three percent discount rate and \$537.90 million at a seven percent discount rate.

T. Regulatory Alternative 3: Upper Boundary—Annualized Costs of the Preferred Alternative

GIPSA then annualized the costs of § 201.3(a) at the upper boundary using both a three percent and seven percent

discount rate and the results appear in the following table. The preferred alternative is also shown for convenience.

TABLE 34—UPPER BOUNDARY OF ANNUALIZED COSTS—SMALL BUSINESS EXEMPTION

Discount rate	Preferred alternative (\$ millions)	Small business exemption (\$ millions)
3 Percent .....	96.01	74.44
7 Percent .....	98.60	76.58

GIPSA expects the annualized costs of § 201.3(a) at the upper boundary with a small business exemption to be \$74.44 million at a three percent discount rate and \$76.58 million at a seven percent discount rate.

U. Regulatory Alternative 3: Point Estimates—Annualized Costs of the Small Business Exemption

Using the same methodology, GIPSA also estimated the point estimates of the annualized costs of § 201.3(a) with a

small business exemption using both a three percent and seven percent discount rate and the results appear in the following table. The preferred alternative is also shown for convenience.

TABLE 35—POINT ESTIMATE OF ANNUALIZED COSTS—SMALL BUSINESS EXEMPTION

Discount rate	Preferred alternative (\$ millions)	Small business exemption (\$ millions)
3 Percent .....	51.44	40.11
7 Percent .....	52.86	41.29

GIPSA expects the annualized costs of § 201.3(a) at the point estimates with a small business exemption to be \$40.11 million at a three percent discount rate and \$41.29 million at a seven percent discount rate.

V. Regulatory Alternative 3: Range of Annualized Costs of the Small Business Exemption

The following table shows the range of the annualized costs of § 201.3(a) at

both a three percent and seven percent discount rate under the small business exemption.

TABLE 36—RANGE OF ANNUALIZED COSTS—SMALL BUSINESS EXEMPTION

Discount rate	Lower boundary (\$ millions)	Point estimate (\$ millions)	Upper boundary (\$ millions)
3 Percent .....	5.79	40.11	74.44
7 Percent .....	6.00	41.29	76.58

GIPSA estimates the annualized costs of § 201.3(a) to range from \$5.79 million to \$74.44 million at the three percent discount rate and from \$6.00 million to \$76.58 million at the seven percent discount rate. The range of potential costs is broad and GIPSA relied on its expertise and the methodology discussed above to arrive at point estimates of the costs within the range that GIPSA expects to occur. GIPSA expects the most likely point estimates of annualized costs to be \$40.11 million at a three percent discount rate and \$41.29 million at a seven percent discount rate.

W. Regulatory Alternative 3: Benefits of the Small Business Exemption

The benefits of § 201.3(a) with a small business exemption are the same as in the preferred alternative except that the benefits for livestock producers, swine production contract growers, and poultry growers will only be captured by those livestock producers, swine production contract growers, and poultry growers selling or growing livestock and poultry for packers, swine contractors, and poultry dealers classified as large businesses.

X. Regulatory Alternative 3: Cost-Benefit Summary of the Small Business Exemption

GIPSA estimates the annualized costs of § 201.3(a) under a small business exemption to range from \$5.79 million to \$74.44 million at the three percent discount rate and from \$6.00 million to \$76.58 million at the seven percent discount rate. GIPSA expects the point estimates of the annualized costs to be \$40.11 million at a three percent discount rate and \$41.29 million at a seven percent discount rate.

Cost-Benefit Comparison of Regulatory Alternatives

The status quo option has zero marginal costs and benefits as GIPSA

does not expect any changes in the cattle, hog, or poultry industries. GIPSA compared the annualized costs of the preferred alternative to the annualized costs of the small business exemption

alternative by subtracting the annualized costs of the small business exemption alternative from the preferred alternative and the results appear in the following table.

TABLE 37—COSTS SAVINGS OF THE SMALL BUSINESS EXEMPTION ALTERNATIVE COMPARED TO THE PREFERRED ALTERNATIVE

Discount rate	Lower boundary (\$ millions)	Point estimate (\$ millions)	Upper boundary (\$ millions)
3 Percent .....	1.08	11.33	21.57
7 Percent .....	1.12	11.57	22.01

The annualized cost savings of the small business exemption alternative is between \$1.08 million and \$21.57 million using a three percent discount rate and between \$1.12 million and \$22.01 million using a seven percent discount rate. At GIPSA’s point estimates, the annualized costs of the small business exemption alternative is \$11.33 million less than the preferred alternative using a three percent discount rate and \$11.57 million less expensive using a seven percent discount rate.

The data presented in Table 4 above show that over 50 percent of broiler growers have only one or two integrators in their local area. This limited integrator choice may accentuate the risks of contracting. Poultry growers with contract growing arrangements with both small and large live poultry dealers face these risks.

Similarly, the potential market failures or unequal bargaining power among contracting parties due to monopsony or oligopsony market power or asymmetric information likely applies to both production and marketing contracts regardless of whether the packer, swine contractor, or live poultry dealer is large or small due to the regional nature of concentration. The result is that the contracts may have detrimental effects on one of the contracting parties and may result in inefficiencies in the marketplace.

One purpose of § 201.3(a) is to mitigate the risks of potential market failures or unequal bargaining power to all livestock producers, swine production contract growers, and poultry growers, not just the livestock producers, swine production contract growers, and poultry growers selling or growing livestock and poultry for large packers, swine contractors, and poultry dealers. The small business exemption would continue to subject the livestock producers, swine production contract growers, and poultry growers with contractual arrangements with small

packers, swine contractors, and live poultry dealers to the contracting risks and potential market failures discussed above. GIPSA believes that the benefits of § 201.3(a) should be captured by all livestock producers, swine production contract growers, and poultry growers.

GIPSA considered three regulatory alternatives and believes the preferred alternative is the best option. All livestock producers, swine production contract growers, and poultry growers, regardless of the size of the firm with which they contract, will capture the benefits of § 201.3(a).

Regulatory Flexibility Analysis of the Preferred Option

The Small Business Administration (SBA) defines small businesses by their North American Industry Classification System Codes (NAICS).<sup>85</sup> SBA considers broiler and turkey producers and swine contractors, NAICS codes 112320, 112330, and 112210 respectively, to be small businesses if sales are less than \$750,000 per year. Live poultry dealers, NAICS 311615, are considered small businesses if they have fewer than 1,250 employees. Beef and pork packers, NAICS 311611, are defined as small businesses if they have fewer than 1,000 employees.

The Census of Agriculture (Census) indicates there were 558 farms that sold their own hogs and pigs in 2012 and that identified themselves as contractors or integrators. The Census provides the number of head sold from their own operations by size classes for swine contractors, but not the value of sales nor number of head sold from the farms of the contracted production. Thus, to estimate the entity size and average per-entity revenue by the SBA classification, the average value per head for sales of all swine operations is multiplied by production values for firms in the Census size classes for swine

contractors. The estimates reveal that although about 65 percent of swine contractors had sales of less than \$750,000 in 2012 and would have been classified as small businesses, these small businesses accounted for only 2.8 percent of the hogs produced under production contracts. Additionally, there were 8,031 swine producers in 2012 with swine contracts and about half of these producers would have been classified as small businesses.

Currently, there are 133 live poultry dealers that would be subject to § 201.3(a). According to U.S. Census data on County Business Patterns, there were 74 live poultry dealers that had more than 1,250 employees in 2013. The difference yields approximately 59 live poultry dealers that have fewer than 1,250 employees and would be considered as small businesses that would be subject to the interim final regulation.

GIPSA records for 2014 indicated there were 21,925 poultry production contracts in effect, of which 13,370, or 61 percent, were held by the largest six live poultry dealers, and 90 percent (19,673) were held by the largest 25 firms. These 25 firms are all in the large business SBA category, whereas the 21,925 poultry growers holding the other end of the contracts are almost all small businesses by SBA’s definitions.

Poultry dealers classified as large businesses are responsible for about 89.7 percent of the poultry contracts. Assuming that small businesses will bear 10.3 percent of the costs in the first full year § 201.3(a) is effective, between \$590,000<sup>86</sup> at the lower boundary and \$3.7 million<sup>87</sup> at the upper boundary in additional costs would fall on live poultry dealers classified as small businesses. This amounts to average

<sup>86</sup> Lower bound cost estimate of \$5.74 million (Table 12) × 10.27 percent of firms that are small businesses = \$589 thousand.

<sup>87</sup> Upper bound cost estimate of \$35.87 million (Table 20) × 10.27 percent of firms that are small businesses = \$3.7 million.

<sup>85</sup> See: [http://www.sba.gov/idc/groups/public/documents/sba\\_homepage/serv\\_sstd\\_tablepdf.pdf](http://www.sba.gov/idc/groups/public/documents/sba_homepage/serv_sstd_tablepdf.pdf). Accessed on September 19, 2016.

estimated costs for each live poultry dealer classified as a small business of between \$10,000 and \$62,400.

As of June 2016, GIPSA records identified 359 beef and pork packers actively purchasing cattle or hogs for slaughter. Many firms slaughtered more than one species of livestock. Of the 359 beef and pork packers, 161 processed both cattle and hogs, 132 processed cattle but not hogs, and 66 processed hogs but not cattle. GIPSA records had a total of 293 cattle slaughterers and 227 hog slaughterers. Two hundred eighty-seven of the cattle slaughterers and 219 of the hog slaughterers would be classified as small businesses.

GIPSA estimates that small businesses accounted for 19.3 percent of the cattle and 17.8 percent of the hogs slaughtered in 2015. If the costs of implementing § 201.3(a) are proportional to the number of head processed, then in 2017, the first full year the regulation would be effective, GIPSA expects between \$507,000<sup>88</sup> and \$5.4 million<sup>89</sup> in additional costs would fall on beef packers classified as small businesses.

This amounts to a range of \$1,800 to \$18,900 for each beef packer classified as a small business. GIPSA expects, between \$13,000<sup>90</sup> and \$308,000<sup>91</sup> would fall on pork packers classified as small businesses, and between \$12,500<sup>92</sup> and \$301,000<sup>93</sup> would fall on swine contractors classified as small businesses. This amounts to average estimated costs for each pork packer classified as a small business of between \$60 and \$1,400, and for each swine contractor classified as a small business of between \$35 and \$831 in the first full year the regulation would be effective.

Annualized ten-year costs discounted at a three percent interest rate would fall between \$392,000 and \$8.7 million for the cattle industry, between \$20,000 and \$772,000 for the hog industry, and between \$456,000 and \$3.6 million for the poultry industry. This amounts to average estimated costs ranging from \$1,400 to \$30,400 for each beef packer, \$45 to \$1,800 for each pork packer, \$27 to \$1,053 for each swine contractor, and \$7,700 to \$61,000 for each live poultry dealer that is a small business. The total

annualized ten-year costs for small businesses would be between \$870,000 and \$13.1 million.

Annualized ten-year costs discounted at a seven percent interest rate would fall between \$406,000 and \$8.8 million for the cattle industry, \$20,000 and \$785,000 for the hog industry, and \$473,000 and \$3.8 million for the poultry industry. This amounts to average estimate costs ranging from \$1,400 to \$30,700 for each beef packer, \$40 to \$1,800 for each pork packer, \$23 to \$1,100 for each swine contractor, and \$8,000 to \$64,100 for each live poultry dealer that is a small business. The total annualized ten-year costs for small businesses would be between \$900,000 and \$13.4 million.

The table below lists the expected additional costs associated with the proposed regulation and upper and lower bound estimates of the costs. It also lists the point estimate, upper bound, and lower bound annualized costs at three percent and seven percent interest rates.

TABLE 38—UPPER AND LOWER BOUND COSTS TO SMALL BUSINESSES OF § 201.3(a)

Estimate type	Cattle (\$ millions)	Hogs (\$ millions)	Poultry (\$ millions)	Total (\$ millions)
First Year Costs:				
Lower Bound .....	0.507	0.025	0.590	1.122
Point Estimate .....	2.969	0.317	2.137	5.423
Upper Bound .....	5.430	0.609	3.684	9.723
10 years annualized at 3%:				
Lower Bound .....	0.392	0.020	0.456	0.867
Point Estimate .....	4.554	0.396	2.026	6.976
Upper Bound .....	8.716	0.772	3.596	13.084
10 years annualized at 7%:				
Lower Bound .....	0.406	0.020	0.473	0.899
Point Estimate .....	4.613	0.403	2.126	7.142
Upper Bound .....	8.820	0.785	3.780	13.385

In considering the impact on small businesses, GIPSA considered the average costs and revenues of each small business impacted by § 201.3(a).

The number of small businesses impacted by § 201.3(a), by NAICS code, as well as the per entity, first-year and annualized costs at both the three

percent and seven percent discount rates appear in the following table.

<sup>88</sup> Lower bound cost estimate of \$2.63 million × 19.3 percent of slaughter in small businesses = \$507 thousand.

<sup>89</sup> Upper bound cost estimate of \$28.14 million × 19.3 percent of slaughter in small businesses = \$5.4 million.

<sup>90</sup> Lower bound cost estimate of \$520 thousand × 17.8 percent of slaughter in small business × 13.8 percent of costs attributed to packers = \$13,000.

<sup>91</sup> Upper bound cost estimate of \$12.49 million × 17.8 percent of slaughter in small business × 13.8 percent of costs attributed to packers = \$308 thousand.

<sup>92</sup> Lower bound cost estimate of \$520 thousand × 2.8 percent of contracted hogs produced by swine contractors that are small businesses × 86.2 percent of costs attributed to swine contractors = \$12,500.

<sup>93</sup> Upper bound cost estimate of \$12.49 million × 2.8 percent of contracted hogs produced by swine contractors that are small businesses × 86.2 percent of costs attributed to swine contractors = \$301 thousand.

TABLE 39—PER ENTITY UPPER AND LOWER BOUND COSTS TO SMALL BUSINESSES OF § 201.3(a)

NAICS	Number of small business	Average cost per entity					
		First-year		Annualized costs 3%		Annualized costs 7%	
		Low (\$)	High (\$)	Low (\$)	High (\$)	Low (\$)	High (\$)
112210—Swine Contractor .....	363	35	831	27	1,053	23	1,071
311615—Poultry .....	59	9,996	62,443	7,727	60,957	8,010	64,066
311611—Cattle .....	287	1,767	18,920	1,366	30,369	1,416	30,732
311611—Hogs .....	219	59	1,405	45	1,781	47	1,811

The following table compares the average per entity first-year cost of § 201.3(a) to the average revenue per establishment for all firms in the same NAICS code.

TABLE 40—COMPARISON OF PER ENTITY FIRST-YEAR COST TO SMALL BUSINESSES OF § 201.3(a) TO REVENUES

NAICS	Number of small business	Average first-year cost per entity		Average revenue per establishment (\$)	Cost as percent of revenue	
		Low (\$)	High (\$)		Low	High
112210—Swine Contractor .....	363	35	831	485,860	0.01	0.17
311615—Poultry .....	59	9,996	62,443	13,842,548	0.07	0.45
311611—Cattle .....	287	1,767	18,920	6,882,205	0.03	0.27
311611—Hogs .....	219	59	1,405	6,882,205	0.00	0.02

The following table compares the average per entity annualized cost at a seven percent discount rate of § 201.3(a) to the average revenue per establishment for all firms in the same NAICS code. The annualized costs are slightly higher at the seven percent rate than at the three percent rate, so only the seven percent rate is shown as it is the higher annualized cost.

TABLE 41—COMPARISON OF PER ENTITY ANNUALIZED COST TO SMALL BUSINESSES OF § 201.3(a) TO REVENUES

NAICS	Number of small business	Average annualized cost per entity		Average revenue per establishment (\$)	Cost as percent of revenue	
		Low (\$)	High (\$)		Low (%)	High (%)
112210—Swine Contractor .....	363	23	1,071	485,860	0.00	0.22
311615—Poultry .....	59	8,010	64,066	13,842,548	0.06	0.46
311611—Cattle .....	287	1,416	30,732	6,882,205	0.02	0.45
311611—Hogs .....	219	39	1,811	6,882,205	0.00	0.03

The revenue figures in the above table come from Census data for live poultry dealers and cattle and hog slaughterers, NAICS codes 311615 and 311611, respectively.<sup>94</sup> As discussed above, the Census provides the number of head sold by size classes for farms that sold their own hogs and pigs in 2012 and that identified themselves as contractors or integrators, but not the value of sales nor the number of head sold from the farms of the contracted production. Thus, to estimate average revenue per establishment, GIPSA used the estimated average value per head for

sales of all swine operations and the production values for firms in the Census size classes for swine contractors

As the results in Tables 40 and 41 demonstrate, the costs of § 201.3(a) as a percent of revenue are small as they are less than one percent, with the exception of the upper boundary for swine contractors.<sup>95</sup>

Annualized costs savings of exempting small businesses would be between \$870,000 and \$13.1 million using a three percent discount rate and

between \$900,000 and \$13.4 million using a seven percent discount rate. At GIPSA's point estimates, the annualized costs of the small business exemption alternative is \$7.0 million less than the preferred alternative using a three percent discount rate and \$7.1 million less expensive using a seven percent discount rate.

Exempting small businesses would continue to subject the livestock producers, swine production contract growers, and poultry growers with contractual arrangements with small packers, swine contractors, and live poultry dealers to the contracting risks and potential market failures discussed above. GIPSA believes that the benefits

<sup>94</sup> Source: <http://www.census.gov/data/tables/2012/econ/susb/2012-susb-annual.html>. Accessed on November 29, 2016.

<sup>95</sup> There are significant differences in average revenues between swine contractors and cattle, hog, and poultry processors, resulting from the difference in SBA thresholds.

of § 201.3(a) should be captured by all livestock producers, swine production contract growers, and poultry growers.

Based on the above analyses regarding § 201.3(a), GIPSA certifies that this rule is not expected to have a significant economic impact on a substantial number of small business entities as defined in the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*). While confident in this certification, GIPSA acknowledges that individual businesses may have relevant data to supplement our analysis. We would encourage small stakeholders to submit any relevant data during the comment period.

#### B. Executive Order 12988

This interim final rule has been reviewed under Executive Order 12988, Civil Justice Reform. These actions are not intended to have retroactive effect, although in some instances they merely reiterate GIPSA's previous interpretation of the P&S Act. This interim final rule will not pre-empt state or local laws, regulations, or policies, unless they present an irreconcilable conflict with this rule. There are no administrative procedures that must be exhausted prior to any judicial challenge to the provisions of this rule. Nothing in this interim final rule is intended to interfere with a person's right to enforce liability against any person subject to the P&S Act under authority granted in section 308 of the P&S Act.

#### C. Executive Order 13175

This rule has been reviewed in accordance with the requirements of Executive Order 13175, "Consultation and Coordination with Indian Tribal Governments." Executive Order 13175 requires Federal agencies to consult and coordinate with tribes on a government-to-government basis on policies that have tribal implications, including regulations, legislative comments or proposed legislation, and other policy statements or actions that have substantial direct effects on one or more Indian tribes, on the relationship between the Federal Government and Indian tribes or the distribution of power and responsibilities between the Federal Government and Indian tribes.

Although GIPSA has assessed the impact of this rule on Indian tribes and determined that this rule does not, to our knowledge, have tribal implications that require tribal consultation under Executive Order 13175, GIPSA offered opportunities to meet with representatives from Tribal Governments during the comment period for the proposed rule (June 22 to

November 22, 2010) with specific opportunities in Rapid City, South Dakota, on October 28, 2010, and Oklahoma City, Oklahoma on November 3, 2010. All tribal headquarters were invited to participate in these venues for consultation. GIPSA has received no specific indication that the rule will have tribal implications and has received no further requests for consultation as of the date of this publication. If a Tribe requests consultation, GIPSA will work with the Office of Tribal Relations to ensure meaningful consultation is provided where changes, additions, and modifications herein are not expressly mandated by Congress.

#### D. Paperwork Reduction Act

This interim final rule does not contain new or amended information collection requirements subject to the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*). It does not involve collection of new or additional information by the federal government.

#### E. E-Government Act Compliance

GIPSA is committed to compliance with the E-Government Act, to promote the use of the Internet and other information technologies to provide increased opportunities for citizen access to Government information and services, and for other purposes.

#### List of Subjects in 9 CFR Part 201

Contracts, Livestock, Poultry, Trade practices.

For the reasons set forth in the preamble, we amend 9 CFR part 201 as follows:

#### PART 201—REGULATIONS UNDER THE PACKERS AND STOCKYARDS ACT

■ 1. The authority citation for part 201 continues to read as follows:

**Authority:** 7 U.S.C. 181–229c.

■ 2. Section 201.3 is amended by redesignating the existing text as paragraph (b), adding new paragraph (a), and adding a heading to paragraph (b) to read as follows:

#### § 201.3 Applicability of regulations in this part.

(a) *Scope of sections 202(a) and (b) of the Act.* The appropriate application of sections 202(a) and (b) of the Act depends on the nature and circumstances of the challenged conduct or action. A finding that the challenged conduct or action adversely affects or is likely to adversely affect competition is not necessary in all cases. Certain conduct or action can be

found to violate sections 202(a) and/or (b) of the Act without a finding of harm or likely harm to competition.

(b) *Effective dates.* \* \* \*

**Larry Mitchell,**

*Administrator, Grain Inspection, Packers and Stockyards Administration.*

[FR Doc. 2016–30424 Filed 12–19–16; 8:45 am]

**BILLING CODE 3410-KD-P**

## DEPARTMENT OF THE TREASURY

### Office of the Comptroller of the Currency

#### 12 CFR Part 51

[Docket ID OCC–2016–0017]

RIN 1557–AE07

### Receiverships for Uninsured National Banks

**AGENCY:** Office of the Comptroller of the Currency, Treasury.

**ACTION:** Final rule.

**SUMMARY:** The Office of the Comptroller of the Currency (OCC) is adopting a final rule addressing the conduct of receiverships for national banks that are not insured by the Federal Deposit Insurance Corporation (FDIC) (uninsured banks) and for which the FDIC would not be appointed as receiver. The final rule implements the provisions of the National Bank Act (NBA) that provide the legal framework for receiverships of such institutions. The final rule adopts the rule as proposed without change.

**DATES:** This final rule is effective on January 19, 2017.

**FOR FURTHER INFORMATION CONTACT:** Mitchell Plave, Special Counsel, Legislative and Regulatory Activities Division, (202) 649–5490, or for persons who are deaf or hard of hearing, TTY, (202) 649–5597, or Richard Cleva, Senior Counsel, Bank Activities and Structure Division, (202) 649–5500, Office of the Comptroller of the Currency, 400 7th Street SW., Washington, DC 20219.

#### SUPPLEMENTARY INFORMATION:

##### I. Introduction

On September 13, 2016, the OCC published a proposed rule to implement the provisions of the NBA that provide the legal framework for receiverships for uninsured banks,<sup>1</sup> 12 U.S.C. 191–200,

<sup>1</sup> All Federal savings associations (FSAs), including trust-only FSAs, are required to be insured. For this reason, this final rule does not apply to FSAs, given that receiverships for FSAs would be conducted by the FDIC.