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AGRICULTURE CONCENTRATION AND COMPETITION

HEARING

BEFORE THE

COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY UNITED STATES SENATE SUBCOMMITTEE ON RESEARCH, NUTRITION AND GENERAL LEGISLATION

ONE HUNDRED SIXTH CONGRESS

SECOND SESSION

ON

AGRICULTURE CONCENTRATION AND COMPETITION

APRIL 27, 2000

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AGRICULTURE CONCENTRATION AND COMPETITION

THURSDAY, APRIL 27, 2000

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

The Committee met, pursuant to notice, at 9:30 a.m., in room SD–106, Dirksen Senate Office Building, Hon. Richard G. Lugar, (Chairman of the Committee,) presiding.

Present or submitting a statement: Senators Lugar, Roberts, Fitzgerald, Grassley, Harkin, Leahy, Conrad, Daschle, Baucus, Kerrey, Johnson, and Burns.

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

The CHAIRMAN. Let me now proceed to our second item of business and a very important one. Today, the Senate Agriculture Committee will conduct the fourth in a series of hearings in this Congress addressing Concentration and Competition in Agriculture.

The Committee has previously heard testimony outlining the potential costs and benefits accompanying consolidation and coordination in agriculture. Witnesses have told us that the benefits include higher quality products available at lower consumer prices and more efficient use of production resources, enabling those resources to move production of other products, thus increasing the national living standard. On the cost side, witnesses have testified that consolidation has negative impacts on environmental quality, on economic viability of small farm and firm operations and rural communities dependent on agriculture.

The Committee has received testimony from Joel Klein, the Assistant Attorney General for Antitrust at the Department of Justice. Mr. Klein has told the Committee that the Department of Justice possesses adequate authority to execute antitrust laws. The question is using them properly. However, recent consolidations continue to raise questions about concentration and antitrust enforcement.

Today's hearing will explore what tools are necessary to facilitate the enforcement of laws prohibiting unfair business practices and which Federal agency is best suited to execute these laws. The Committee will also consider what role the United States Department of Agriculture should play in the agribusiness merger review process.

Currently, reviews of mergers and acquisitions within the agribusiness sector occurs with the Federal Trade Commission and the Department of Justice. These agencies often call upon USDA to provide expertise and data on pending reviews. There are proposals before the Committee which formalize USDA's role in the merger review process. These proposals do other things, such as establishing a commission to review claims of family farmers and ranchers who have suffered financial damages due to unfair business practices. Also, these proposals require large agribusiness to report on their corporate structure describing the domestic and foreign activities of these firms.

[The prepared statement of Senator Lugar can be found in the appendix on page 64.]

Mr. John Nannes, the Deputy Assistant Attorney General of the Department of Justice, will provide the Committee with a progress report on the newly created position of Special Counsel for Agriculture within the Department of Justice.

I will welcome in due course also Mr. James Rill, formerly the Assistant Attorney General for Antitrust, and who more recently was appointed by the Attorney General as chair of the International Competition Policy Advisory Committee, whose final report was completed in February.

We welcome Mr. David Nelson from Credit Suisse First Boston. Mr. Nelson will provide the Committee with an analysis of the performance of agribusiness on Wall Street.

Also presenting testimony are Dr. Stephen Koontz from Colorado State University and Mr. Peter Carstensen from the University of Wisconsin. Both have done extensive research on the issues of agricultural concentration and antitrust law.

A third panel today will contain Mr. Ron Warfield from Gibson City, Illinois, representing the American Farm Bureau Federation; Mr. Leland Swenson from Aurora, Colorado, President of the National Farmers Union; Mr. John Greig from Estherville, Iowa, representing the National Cattlemen's Beef Association; and Mr. Jon Caspers from Swaledale, Iowa, representing the National Pork Producers Council.

It is a privilege to have you, Mr. Nannes, and before I ask you for your testimony, I would like to recognize the distinguished Ranking Member of the Committee for an opening statement.

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

Senator HARKIN. Thank you very much, Mr. Chairman. There certainly is no issue raising more concerns in agriculture today than the topic of this hearing. The structure of agriculture and the entire agribusiness and food sector is being massively transformed and the pace is accelerating. So I commend you, Mr. Chairman, for holding today's hearing. I look forward to working with you to shape effective policies to deal with the consolidation and economic concentration in agriculture.

But we are quickly running out of time. Unless we change course, the independent family farm is on the path to extinction. Independent farmers can compete and thrive if—if the competition

is based on productive efficiency and delivering abundant supplies of quality products at reasonable prices. But no matter how efficient farmers are, they cannot survive a contest based on who wields the most economic power. Farmers suffer from a gross inequality in economic strength, and as a consequence, they receive lower returns than they would if the markets were truly fair, open, and competitive.

While the market basket of food has only increased by three percent since 1984—think about that, the market basket of food has only increased by three percent since 1984—the farm value of that market basket has plummeted 38-percent. The farmers' share of the retail food dollar has dropped from 47-percent in 1950 to 21-percent last year.

Consumers are also at the mercy of a few large firms situated between them and farmers. I have always likened the arrangement to an hourglass. You have got a lot of producers on one side, a lot of consumers on the other side, and then you have got a choke point right in the middle, a few large agribusiness firms. Well, I believe we have to stop this trend now before it builds up more momentum and heads further down the slippery slope towards consolidation and integration where independent farmers become a footnote in history.

I think there are three things that must be done. First, we must start with strong enforcement of existing laws to protect fair, open, and competitive markets.

Second, Congress must enact legislation to provide authority to ensure these fair and open and competitive markets in our food and agriculture industry, and I do commend this administration for breathing new life into antitrust enforcement in recent years. However, we are still suffering the fallout from years of lax antitrust enforcement and misguided court decisions that have sapped the strength of the Sherman and Clayton Acts as they were originally intended. We must correct this situation with new legislation.

Several of us have introduced the Farmers and Ranchers Fair Competition Act of 2000 to expand the Secretary of Agriculture's authority to prohibit anti-competitive practices and mergers by agribusinesses that damage small and medium-sized farms.

Third, we must also help farmers improve their position relative to the powerful firms they deal with in the evolving agricultural markets. That includes assisting them in gaining a share of the profits made from processing and adding value to crops and livestock after they leave the farm. Farmers ought to get a share of those profits, also.

But lastly, we must deal with these issues in a comprehensive way to ensure that independent farmers are not harmed by the practices of large agribusinesses and that market concentration does not undermine the ability of farmers to compete in the marketplace.

Mr. Chairman, again, I commend you for holding these hearings and hopefully we can move ahead this year yet with some legislation to address this problem.

The CHAIRMAN. Thank you very much, Senator Harkin.

The Chair will recognize each Senator for hopefully a short opening statement. It has always been our policy that Senators want to

be heard on these issues, but hopefully they can be heard fairly briefly because we have a number of panels. So I will recognize now Senator Grassley.

STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM IOWA

Senator GRASSLEY. Mr. Chairman, your admonition, it was my understanding that Senator Leahy and Senator Daschle and myself would have an opportunity to present some points of view on our bill, or is that not the way you had intended?

The CHAIRMAN. No, I think you ought to do that. That is really a part of our hearing.

Senator GRASSLEY. As we all know, attention on agricultural concentration has become especially focused within the last 18-months to 2-years. Record low prices for many agricultural commodities and a wave of agribusiness mergers have led anyone who is deeply involved in agriculture to take a serious look at infrastructure of agriculture and whether it is conducive to the survival of small independent producers.

My bill would require the Department of Agriculture to do a review of proposed agriculture mergers. The U.S. Department of Agriculture would have the mission of assessing whether a proposed merger would have a substantial detrimental effect on producers' access to the marketplace. This review would be conducted simultaneously with the review done by the Department of Justice.

Furthermore, my bill makes no changes in the antitrust review process or the standard that is presently conducted by the Department of Justice. If the USDA believes the merger would have a substantial detrimental impact on farmers' access to the marketplace, then the USDA would be able to enter into discussions with the merging parties to address those concerns. If those discussions are not successful, my bill gives the USDA a very narrow time frame in which to decide whether or not to pursue a challenge to the merger, even if the Department of Justice has approved the merger. If USDA does go forward with a challenge, then the Department must make its case in Federal court. If the Department wins the impartial forum of the Federal court, then the merger is stopped or conditions are imposed on the transaction.

My bill also calls for the appointment of a special counsel for competition matters at the USDA and an assistant Attorney General for agricultural antitrust matters at the Department of Justice.

The legislation also expands the authority of the USDA's packers and stockyards division to investigate anti-competitive, unfair, or monopolistic practices in all commodities, because currently the packers and stockyards authority pertains only to the livestock industry.

My bill has been quite controversial. Some believe that my bill is anti-agribusiness. However, I have worked on a farm practically all my life. I made my living as a farmer before I came to the Congress and no one knows better than I do that a farmer cannot do his job without the agribusiness that produces the seed, fertilizer, pesticides, and equipment necessary to produce a crop. A livestock producer cannot get his product to consumers without the agri-

business that processes those animals into cuts of meat to be sold at the retail level. I know as well as anyone that agriculture cannot survive without agribusiness. I do not believe that my bill imposes an undue burden on this agribusiness.

I have heard it said that allowing USDA into the merger review process, as my bill does, politicizes the process. But my legislation does not give USDA a rubber stamp to stop mergers. The only requirements that my bill places on USDA is for them to do a merger assessment based upon farmer impact standard. My bill encourages the U.S. Department of Agriculture to work with merging parties to work out any concerns. It would do so without disrupting or displacing the process currently used by Justice and the FTC. I emphasize, no merger can be stopped without a determination of an impartial Federal court that the USDA has met the standards set by my legislation.

Bringing the Department of Agriculture into the merger review process is not unprecedented, because currently, under a memo of understanding, the U.S. Department of Agriculture and Justice consult and discuss with respect to agriculture mergers. My bill would formalize this process, make it more open and consistent. Furthermore, other agencies such as the FCC and the Surface Transportation Board play integral roles in communication and railroad mergers, respectfully, giving the USDA a prominent role in these reviews and it is not unprecedented.

It has also been implied that the bill would affect all businesses. I want to make it clear that my bill pertains only to agriculture. Agriculture concentration is one of the top issues that I hear about from producers in my State and agriculture is vital to my State's economy.

The bill would not drag the merger review process out. It requires USDA to conduct its farmer impact assessment within the same time period as Justice merger review. Because USDA represents farmers, my legislation guarantees farmers a place at the table when mergers in their industry are considered without making the process intolerably burdened.

I want to reiterate my belief, Mr. Chairman, that the bill makes the agriculture merger review process more open and consistent in a way that is fair both to producers and agribusiness. I have said many times that I want to see a meaningful action on agriculture concentration taken in this Congress and I am committed to that goal.

Certainly, I believe there are ways in which my bill can be improved, and I am willing to listen to others' concerns and suggestions. But I will continue to push for Congressional action on agriculture concentration so long as this Congress is in session. The issue is too important to so many producers for it to be dropped. I know that many in the agribusiness community have been advocating a "just say no" approach to agriculture concentration merger. For me and, I believe, other members, this do nothing approach is not acceptable. So I urge the agribusiness community who have worked with me on many occasions to come to Congress with constructive proposals on how to guarantee agriculture mergers that their concerns are heard when agriculture mergers are considered.

I want to commend Senator Daschle and Senator Leahy for their hard work and for bringing forward a substantive initiative, as well, and would relish the opportunity to visit with them about ways in which our legislation could be worked out.

Lastly, as strictly a Republican member of this committee, I would like to suggest that my bill is offered in the tradition of our party's feeling that the Government should be a referee in our economy, and that philosophy has been a part of our party's position since Teddy Roosevelt.

[The prepared statement of Senator Grassley can be found in the appendix on page 66.]

The CHAIRMAN. Thank you very much, Senator Grassley.

Senator Leahy.

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

Senator LEAHY. Mr. Chairman, I am glad you are having this hearing. I think it is an extremely important one. As Senator Grassley has pointed out, you have two members of the Judiciary Committee here, both Senator Grassley and myself. His bill is an excellent one. It is before the Judiciary Committee. I am hoping that we are going to have hearings that might move forward on that as I do here. The bipartisan bill that I worked on with the Democratic leader, Senator Daschle, and other members of the Committee, we were helped by the American Farm Bureau Federation and the National Farmers Union in this.

Basically, what we were saying is that family farmers and ranchers should be the key focus of our competition, our agricultural competition policies, because there is really not a level playing field in American agriculture today. Give us a level playing field and I will stack up American agriculture against anywhere in the world. But on one side, we have got the agribusinesses that can raise billions of dollars on Wall Street by a click of a computer by issuing stock, whether valued at what you paid for it or not. On the other side, you have got family farmers and ranchers. They have little or no bargaining power and they cannot issue stock.

I just do not want agri-corporate giants hitting farmers over the head with unfair and discriminatory and deceptive practices. I am fed up with the "sign here or you lose your farm" contracts. I am fed up with the "take my price or lose your ranch" deals. I am fed up with deceptive practices by processors to cheat farmers out of a fair chance to compete. I look at the editorials which we will have in the record.

One of our papers wrote about Suisse, which controls 70-percent of the milk market in New England. I look at what the Commissioner of Agriculture of Massachusetts wrote. He said in a recent letter that Suisse Foods' milk processing capacity approaches 80-percent of the Massachusetts market, and they may have entered into an exclusive agreement with a major supermarket to exclude a competitor's milk from its shelves. Well, that does not help consumers, and it certainly does not help producers and somebody has to say, enough is enough. So we have asked to enhance competition in rural America by increasing the bargaining power of family-sized

farmers and ranchers, giving the Secretary of Agriculture the power to move more quickly.

I will put my whole statement in the record, Mr. Chairman, but I think this hearing is extremely important, and ironically enough, I and, I assume, Senator Grassley will have to leave to go to that same Judiciary Committee. But I intend to continue to work with Senator Grassley and the Judiciary Committee on that and with Senator Daschle and the others on the Committee here, and with you, of course.

The CHAIRMAN. Thank you very much, Senator Leahy.

Senator GRASSLEY. Mr. Chairman, could I tell Senator Leahy that I am going to send a letter today to Senator Hatch, Chairman of the full Committee, Senator Mike DeWine, Chairman of the Antitrust Subcommittee, requesting such a hearing.

Senator LEAHY. I will join you on that, if you would like.

Senator GRASSLEY. If we have not sent it, I will have you join me on it.

Senator LEAHY. Thank you.

Senator GRASSLEY. It is good to facilitate communication here in the Judiciary Committee.

Senator LEAHY. We come to the Agriculture Committee to facilitate the Judiciary Committee.

The CHAIRMAN. Exactly. Senator Roberts.

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

Senator ROBERTS. Mr. Chairman, first, I want to thank you for arranging this room. I hope this is the new home of the Agriculture Committee. It is certainly befitting your stature and I think Senator Leahy's portrait would go fine right up on that wall.

[Laughter.]

Senator CONRAD. We have got a spot for his portrait over on the House side. We are working very hard on it.

Senator LEAHY. It is an elevator shaft.

[Laughter.]

Senator ROBERTS. Mine has already been taken down. That is how that works.

Mr. Chairman, if I could reserve my time, as I indicated to you, there is an Emerging Threat Subcommittee of the Armed Services Committee of which I am privileged to chair with a markup at 10:00, but I could probably go about 10:10 and we could put that off. I see that the distinguished Democratic leader is here and I know his schedule is extremely busy. If he would like to go at this particular time, if I could reserve my time to follow him, I would be more than happy to do so.

The CHAIRMAN. Very well. The Democratic leader.

Senator DASCHLE. I am very grateful to you. I can wait my turn. You have a schedule, too, and I am planning to be here for a little while, but I very much appreciate your graciousness.

Senator ROBERTS. Thank you, Mr. Chairman. Mr. Chairman, thank you for holding this hearing today. I have a short statement and a few questions to read because I have to leave, and I will try to do that as quickly as I can.

In regard to the issues involving debate on concentration in agriculture and agribusiness, this is a most important and very crucial debate. During the past few years, as has been said by my colleagues, the general economy and the stock market have been booming while the agriculture economy has gone through some very, very difficult times. At the same time we have experienced this downturn in the agriculture economy, we have seen mergers or proposed mergers in the grain business and the hog business, in regards to railroads and the biotech sector. It is imperative that we take a much closer look on these issues.

The purpose of today's hearing is to discuss several bills introduced by members of this committee to address the merger issue and the business practice in this business. These bills include those introduced by Senator Daschle and Leahy, Senator Grassley, and a ban on packer ownership of livestock offered by Senator Johnson. Obviously, these bills would greatly expand the antitrust powers related to agriculture and would expand the USDA oversight.

Now, Mr. Chairman, 3-months ago, you held a hearing on this same issue, and at that time we asked the Department of Justice and the Department of Agriculture and the administration to provide us with their "official positions" on proposals to ban packer ownership of livestock and to expand the antitrust powers related to agriculture. I am not sure about this, Mr. Chairman, but I do not believe any "official position" has been put forth by the administration at this point. However, now that we have the formal proposals introduced on each of these issues, I look forward to, or we should look forward to asking Mr. Nannes with the Department of Justice to provide us with the official administration position on these pieces of legislation. I think that would be helpful.

Also during the hearing in February, I discussed with several of the producer and the farm organization witnesses the current statutory and regulatory powers that the Department of Justice and the USDA have at their disposal. We were in virtual unanimous agreement, Mr. Chairman, that they are not currently using all the powers available to them. I also want to know why this is the case. Do we need more tools in this area? If so, what are they? Are they commensurate with the bills that have been introduced?

Now, going back to last year, we have asked the administration for recommendations in this area as well as their position. Have we received any yet? I will also, and we should also, if I am not present, ask Mr. Nannes for the administration's positions and the recommendations in this area.

Mr. Chairman, I believe the discussion we will have here today is an important discussion that those of us in the agriculture community need to have, make no mistake about that. But again, I want to stress there are several things the members of this committee need to carefully consider when we discuss these issues. We know the problem, but there are some concerns, as well.

We as a committee, with all due respect, have very little expertise in antitrust law. Are we really the ones to be rewriting the books on this issue? I want to applaud Senator Grassley for getting in touch with the distinguished Chairman of the Judiciary Committee in an effort to hold a hearing there.

Is there really a lack of enforcement in the area of mergers in agribusiness? Mr. Nannes' testimony cites several very high-profile cases involving agribusiness where the Department of Justice did take action. But he also points out that the two highest fines ever levied by the Department of Justice for anti-competitive practices and pricing were levied on two firms involved in agribusiness.

What will a virtual absolute halt to agribusiness mergers do to our producers and agribusinesses' ability to compete in the world marketplace? The Senate has already spoken on that issue. What will these proposals do to producers' ability to create new arrangements and to expand their profitability? In Kansas, several cooperatives have joined with Cargill to announce they have come together to form a joint company that would allow them to ship grain more efficiently and to return, hopefully, the higher profits to producers.

The testimony of the National Cattlemen's Beef Association today also mentions the success of an outfit called U.S. Premium Beef in Kansas and mentions a new alliance that is being started in Kansas called Quality Beef. Mr. Chairman, this is an alliance of producers and a major retail firm to control everything in the process from the DNA to the dinner table to provide consumers with a high-quality product.

Does this committee want to stop these forms of producer activities from taking place? Obviously not, but this is the kind of concern that I think we have to take into account. More importantly, why is the USDA not using all the tools it has currently at its disposal in the area of anti-competitive practices?

Mr. Chairman, we are experiencing mergers in all areas of our economy. Do I like all these mergers? No. Do I like some? Yes. But I question the wisdom of some proposals to address these concerns legislatively. I also want to assure that in the zeal of some to ensure some competition in the marketplace, we do not take away the ability of our producers and agribusiness to compete in the domestic and the world markets.

I look forward to working with my colleagues, and again, Mr. Chairman, I will submit these questions for the record. But what is the administration's position on the Daschle–Leahy bill? What is the administration's position on the Grassley bill? What is the position on proposals to ban packer ownership of livestock? What is that position if it is a producer-owned business, even if it is not a cooperative? What are the administration's recommendations, if any, for additional tools that you need in this area?

And one other situation. Your testimony mentions in particular the Cargill-Continental case and several divestitures that you forced to allow the merger to go through. I am not trying to perjure them one way or the other. One of these facilities was in Kansas. I am wondering how the Department of Justice did determine which facilities to divest. Where did the expertise come from to allow you to make those decisions? Hopefully, it is in consultation with the USDA.

We also need to know how Mr. Doug Ross is getting along over in your shop, if he has enough pencils and papers and telephones and money to do the job and to peer over your shoulder to make sure you are doing the job right.

I apologize to my colleagues for the length of the statement and I thank you, Mr. Chairman.

The CHAIRMAN. Thank you very much, Senator Roberts.

Let me identify the distinguished gentleman to your left. Senator Conrad Burns is not a member of the Committee, but he is a good friend of the Committee and he has asked to be able to observe the hearing from the podium and we are delighted that he is here and want to extend that courtesy to the Senator.

Senator Conrad.

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

Senator CONRAD. Thank you, Mr. Chairman. I think we all know that concentration is a significant problem. This chart, I think, sums it up. It shows the concentration, the market share by the top four firms in corn wet milling, wheat flour milling, and soybean crushing, and you can see in corn wet milling, the top four firms control 74-percent, in wheat flour milling, 62-percent, in soybean crushing, now 80-percent.

These are levels of concentration that do threaten those who are sellers. Normally, we think of the problem of antitrust as a question of monopoly. That is a question of where there are few sellers. Monopsony, which is really the problem we are facing here, is a problem of a few buyers, and that is the problem that farmers confront all across America. We have a small number of buyers and the indications are, if you look at the farmers' share of the retail dollar, it is shrinking and shrinking dramatically.

When I went to business school to get a master's in business administration, one of the things they taught us is you get return based on the power you have in the marketing chain, and if there are few buyers and many sellers, the sellers have very little leverage. The buyers have the leverage to control the price. That, I think, is what we are seeing.

It is even more pronounced in the control of regional export markets, where we have four firms controlling 100-percent of some commodities through specific ports. In the case of wheat, the level is 86-percent through the Pacific Northwest ports and 81-percent through the Great Lakes.

Mr. Chairman and members of the Committee, we have an obligation to act. The current laws are not working. I think we could do a better job of enforcing those laws, but clearly, that is not enough. We held a meeting in my office with the Attorney General on a bipartisan basis. I think there were 12-Senators there. Senator Harkin was there. Senator Grassley was there and others. And we made the point to her that there needs to be greater enforcement.

But it also became clear as we met with the top leadership of Justice that we need to do more than that. We need to legislate. That is what the Farmers and Ranchers Fair Competition Act of 2000 does. It is written by Senator Daschle, Senator Leahy, Senator Harkin, and others of us. Senator Grassley also has an excellent bill. Hopefully, we can come together and legislate.

The CHAIRMAN. Thank you very much.

Senator Daschle.

STATEMENT OF HON. THOMAS DASCHLE, A U.S. SENATOR FROM SOUTH DAKOTA

Senator DASCHLE. Mr. Chairman, I want to add my voice to those who have already thanked you for holding this important hearing. I appreciate very much your leadership and your willingness to stay with this issue as you have done over the course of this Congress.

I also have a very lengthy statement that I would ask consent that it be inserted in the record———

The CHAIRMAN. It will be inserted.

Senator DASCHLE.—as well as a point-by-point summary of the bill that has been referred to that we have now introduced. With your willingness to do that, I will just summarize briefly a few points.

I believe that in our lifetimes, we have seen the industrialization of agriculture to the extent that nobody could have forecast. Part of that industrialization can be truly viewed as progress. Part of it, in my view, has been extraordinarily positive for rural communities. But a large part of it also has been very, very detrimental and disconcerting and that is what brings us to this hearing today, in my view.

I think as we look to the industrialization, we see this growing concentration and we recognize that, that is the trend in just about every industry, but it does not have to be inevitable. As we travel to other countries, especially in Europe and Asia, we find that small producers still are viable and are very much a part of the economy. That economy is thriving in agriculture in many parts of the world outside of the United States in rural areas.

I think as we look to the consequences of industrialization in agriculture today, we see many practices within the industry that are very fair and understandable. But as we look closer, we see many which are not fair, and as we look at those which are not fair, we are more and more of a realization that many of those unfair practices are taking place in large measure because we have not created the tools within the Government to assure that this new industrialization in agriculture can be addressed through sound public policy, and that is the essence of the legislation that we have introduced and I think Senator Grassley, as well.

No one should be mislead, and I do not think anyone in this room certainly is. What is happening in agriculture today will have irreparable effect on virtually every entity within rural America today. On farmers and ranchers, when they have the inability to trade fairly their products, whether it is livestock or grain. On the markets themselves and the effect of that concentration. And certainly on communities, when one plant will pull out, leaving a large percentage of any community completely unemployed, as has happened in South Dakota. So those profound consequences are ones that we simply cannot ignore.

Do we have the infrastructure in place to be able to deal with the industrialized agriculture as it exists today? Our view is that we do not. So, in essence, we try to do three things.

First, we strengthen USDA's power to protect all producers from anti-competitive practices. second, we require that the potential impact of proposed mergers on rural communities be considered dur-

ing the process of reviewing these mergers. And then, finally, we begin to restore the fairness that we all hope we can see in the marketplace by increasing the bargaining power of small producers.

But we do so not by taking anything away from the Justice Department. We do so by empowering the Agriculture Department. I think both branches of government, the legislative and executive, need to be involved, and both agencies within the executive branch charged with overseeing this change in our industry ought to be fully empowered, the Justice Department and the Department of Agriculture. This bill addresses what I think is a very serious deficiency in the Department of Agriculture today, and I again thank the Chairman.

[The prepared statement of Senator Daschle can be found in the appendix on page 70.]

The CHAIRMAN. I thank you, Senator Daschle, for your leadership.

Senator Johnson

STATEMENT OF HON. TIM JOHNSON, A U.S. SENATOR FROM SOUTH DAKOTA

Senator JOHNSON. Thank you, Mr. Chairman, for holding this hearing. I appreciate that there are some time concerns and we need to move on to the panel. I think that I will submit a statement relative to my general observations about concentration in the agricultural industry and focus simply in an expeditious fashion on some legislation that I have sponsored which is relevant to the discussions today.

Mr. Chairman, the Rancher Act, S. 1738, is legislation that I have introduced that is bipartisan in nature to prohibit meat packers from owning livestock prior to slaughter. My bill would reign in the meatpackers' leverage over the livestock market and reestablish a free, fair, and competitive atmosphere for independent livestock producers. I have been joined by Senators Kerrey, Grassley, Thomas, Daschle, Harkin, Dorgan, Wellstone, Conrad, and Bingaman in this effort. Representatives Minge and Leach have introduced similar legislation in the other body.

This legislation is endorsed by the National Farmers Union, the South Dakota Farmers Union, the South Dakota Cattlemen, the Center for Rural Affairs, the Organization for Competitive Markets, RCAF, Iowa Pork Producers Association, and the Illinois Farm Bureau.

This legislation recognizes the need for value-added opportunities and exempts producer owned and controlled cooperatives and small producer owned meatpackers from the ownership prohibition.

The legislation is also retroactive, requiring meatpackers to divest of ownership interest in livestock which directly takes on the potential as the Smithfield situation. A recent survey of over 1,000 farmer members of the Iowa Pork Producers Association found that 88-percent support a Federal-level ban on packer ownership of hogs. In South Dakota, our Governor Janklow, a Republican governor, has signed a resolution adopted by the legislature calling for a Federal-level prohibition of packer ownership of livestock. And in Iowa, legislation has passed to strengthen their existing law on

packer ownership and Governor Vilsack there has signed this provision into law recently.

A ban on packer ownership of livestock would not drive packers out of business because most of their earnings are, in fact, generated from branded products and companies marketing directly to consumers. It boils down, Mr. Chairman, to whether we want independent producers in agriculture or if we are going to yield to concentration and see farmers and ranchers become low-wage employees on their own land.

Second, I would observe just quickly that I am very pleased to join Senator Daschle in cosponsorship of S. 2411 that takes on anti-competitive issues in agriculture today. This legislation compliments, I believe, my legislation to ban packer ownership. S. 2411 seeks better cooperation and communication between the Department of Justice and the Department of Agriculture and the bill clarifies that meat packers and others engaged in unjustifiable price discrimination and preferential purchasing are violating the law.

Too many farmers and ranchers feel agribusiness buyers have discriminated against them based on the size of their operations, and so our bill clearly prohibits these practices. In addition, the farmers and ranchers are economically harmed by anti-competitive behavior. This bill establishes a family farmer and rancher claims commission authorizing direct compensation to them. The bill also requires a new USDA analysis of proposed agribusiness mergers to determine if a given merger will have a negative effect on family farmers, market prices, and rural communities.

Since many producers are either coerced or attracted into contract production scenarios, I am pleased that the bill requires basic public disclosure standards for these contracts. A producer needs to know if the contract he or she is signing is worth the paper it is written on. Poultry producers learned the hard way that some contracts are recipes for disaster to the independent farmer.

Finally, in regards to livestock markets, I would like to mention three legislative initiatives related to fair and free competition in the marketplace that I support and encourage Congress to act upon this year. One would be the country origin of meat labeling legislation, which now has 15-bipartisan Senate cosponsors, S. 242, the Meat Labeling Act of 1999, including Senators Baucus, Daschle, Grassley, Harkin, Kerrey, Conrad, Bingaman, Bond, Campbell, Durban, Enzi, Feingold, Graham, Reed, and Thomas. This bill will require a country of origin labeling for muscle cuts and ground products of beef, lamb, and pork.

And then finally, Mr. Chairman, USDA quality grade reform, as S. 241, the Truth in Quality Grading Act of 1999. This bill prohibits imported beef and lamb from displaying USDA quality grade stamps. USDA recently solicited public opinion concerning whether the Secretary should use administrative authority to discontinue using USDA quality grades on imported beef and lamb meat carcasses. This is consistent with the direction of this legislation, and again, I think, is part and parcel of our overall legislative strategy to deal constructively with the problem of concentration, lack of competition, lack of price leverage for independent livestock producers in America.

I think that consideration of these pieces of legislation would be consistent with that more comprehensive strategy. I thank you, Mr. Chairman, for holding this hearing today.

[The prepared statement of Senator Johnson can be found in the appendix on page 73.]

The CHAIRMAN. Thank you, Senator Johnson.

Senator Kerrey.

STATEMENT OF HON. ROBERT KERREY, A U.S. SENATOR FROM NEBRASKA

Senator KERREY. Mr. Chairman, I will just submit a statement for the record and thank you for holding this hearing and hope that the exchange I have heard earlier between Senator Leahy and Senator Grassley is an indication that this Congress will be able to mark up a bill and move a bill this year. I get asked over and over and over at the local and at the State level, why is Congress unable to respond to what the people themselves are saying need to be done in this area, and I am hopeful that we can pass good legislation this year.

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

The CHAIRMAN. I thank the Senator. His statement and that of Senator Johnson will be published in full in the record.

Senator Fitzgerald.

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

Senator FITZGERALD. Thank you, Mr. Chairman. I am not going to have an opening statement and I just want to use this time to welcome a constituent of mine who is going to be on the third panel, Ron Warfield, who is the President of the Illinois Farm Bureau from Gibson City, Illinois. I just want to welcome Ron to the Committee, thank the Chairman for holding these hearings, and I think it is a very important issue and getting more of the details of the two competing bills in this important area should be very beneficial to all the Committee members. Thank you.

The CHAIRMAN. I thank the Senator.

Mr. Nannes, you are recognized.

STATEMENT OF JOHN M. NANNES, DEPUTY ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION, DEPARTMENT OF JUSTICE, WASHINGTON, DC.

Mr. NANNES. Thank you, Mr. Chairman and other members of the Committee. I am pleased to have the opportunity this morning to discuss issues related to antitrust enforcement in the agricultural marketplace.

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

In the midst of these changes, farmers have expressed concern about the levels of competitiveness in agricultural markets. Farmers know that competition at all levels in the production process

leads to better quality, more innovation, and competitive prices. They know, too, how important antitrust enforcement is to assuring competitive markets. Enforcement of the antitrust laws can benefit farmers in their capacity as purchasers of goods and services that allow them to grow crops and to raise livestock, and also in their capacity as sellers of crops and livestock to feed people, not only in our country but throughout the world.

The Antitrust Division takes these concerns seriously and has been very active in enforcing the antitrust laws in the agricultural sector. In conversations with farm groups, we have found that farmers are especially concerned, as some of you have indicated already this morning, about the potential impact of mergers. Farmers are concerned that mergers will limit the number of sellers from whom they buy and will limit the number of customers for crops and livestock to whom they sell. For this reason, I think it may be helpful to start out with a brief review of recent merger enforcement actions that the Antitrust Division has taken in this very important sector of our economy.

In just the last 17-months, the Antitrust Division has challenged four significant mergers that have affected agricultural markets: The proposed acquisition by Monsanto of DeKalb Genetics Corporation, which would have significantly reduced competition in corn seed biotechnology innovation to the detriment of farmers; the proposed acquisition by Cargill of Continental's grain business, which would have significantly reduced competition in the purchase of grain and soybeans from farmers in various local and regional markets; the proposed acquisition by New Holland of Case, which would have significantly reduced competition in the sale of tractors and hay tools to farmers; and the proposed acquisition by Monsanto of Delta and Pine Lane, which would have significantly reduced competition in cottonseed biotechnology to the detriment of farmers.

Certain aspects of these enforcement actions warrant particular attention. In most merger investigations, the Antitrust Division is concerned about the ability of the merging companies to raise above the competitive level the price of products or services they sell.

Of course, it is also possible that a merger will substantially lessen competition with respect to the price that the merging companies pay to purchase products. This latter matter is a particular concern to farmers, who often sell their products to large agribusinesses. For a while, there seems to have been some uncertainty about whether the antitrust enforcement agencies take this possibility into account when analyzing mergers. In fact, our merger guidelines specifically provide that the Antitrust Division will review mergers to determine whether they pose a competitive threat to persons buying goods or services from the merged entity and whether they pose a competitive threat to persons selling goods or services to the merged entity.

This distinction is illustrated by our challenge to the Cargill-Continental transaction last year. The merger affected a number of markets. The parties were sellers of grain and soybeans in the United States and abroad, but they were also buyers of grain and soybeans in various local and regional domestic markets. We

looked at all of the potentially affected markets. We concluded ultimately that the transaction was not problematic on the sell side. The companies did not account for a substantial share of grain or soybean sales in either a national or international market.

However, we concluded that the proposed merger could have depressed prices received by farmers for grain and soybeans in certain regions of the country and we determined that the transaction as proposed should be challenged. It was only after the parties agreed to restructure the transaction with significant divestitures of port, rail, and river facilities that we permitted it to proceed.

Taken as a whole, these four major merger enforcement actions establish certain important propositions. First, the Antitrust Division carefully reviews agricultural mergers for their competitive implications.

Second, if a merger is likely to lead to anti-competitive prices for products purchased by farmers, the Antitrust Division will file suit.

Third, if a merger is likely to lead to anti-competitive prices for products sold by farmers, the Antitrust Division will file suit.

Fourth, the Antitrust Division's concerns are not limited to traditional agricultural products but extend also to biotechnology innovation.

And fifth, while the Antitrust Division will consider proposed divestitures and other forms of relief that permit a merger to proceed as restructured, the Division will not shrink from challenging a merger outright if it concludes that lesser forms of relief are not likely to address fully the competitive problems raised by the merger.

The Division's agriculture enforcement actions have not been limited to mergers. During the same period, the division also criminally prosecuted companies that had fixed prices for products purchased by farmers, and secured numerous criminal convictions and the highest fines in antitrust history.

Beginning in 1996, the Division prosecuted Archer Daniels Midland and others for participating in an international cartel organized to suppress competition for lysine, an important livestock and poultry feed additive. The cartel had inflated the price of this important agricultural input by tens of millions of dollars during the course of the conspiracy. ADM plead guilty and was fined $100 million—at the time, the largest criminal fine in history. Two Japanese and two Korean firms were also prosecuted for their participation in the cartel, and individual corporate employees were prosecuted and received substantial jail sentences.

Last year, the Division prosecuted the Swiss pharmaceutical giant F. Hoffman-LaRoche and a German firm, BASF, for their roles in a decade-long worldwide conspiracy to fix prices and allocate sales with respect to vitamins used as food and animal feed additives and nutritional supplements. The vitamin conspiracy affected billions of dollars of U.S. commerce. Hoffman-LaRoche and BASF pled guilty and were fined $500 million and $200 million, respectively. These are the largest and second-largest fines in history. In fact, the $500 million fine is the largest criminal fine ever imposed in any Justice Department proceeding under any statute. Six executives from Switzerland and Germany pled guilty and will serve substantial jail sentences in the United States.

The Antitrust Division will prosecute companies for price fixing whenever and however we learn of it. The lysine and vitamin cases get publicity because of the prominence of the companies involved and the amount of commerce at stake, but we also successfully prosecuted two cattle buyers in Nebraska a few years ago for bid rigging in connection with procurement of cattle for a meat packer after an investigation was conducted with the valuable assistance of the Department of Agriculture, which was looking at the same conduct under its statute.

In short, we have brought and will continue to bring charges against companies that engage in criminal behavior that adversely affects farmers.

The Division also investigates other forms of business behavior that may have anti competitive effects. Such conduct may constitute an illegal restraint of trade or, in some circumstances, monopolization or attempted monopolization. The Division is, in fact, conducting a number of civil investigations right now in which we are considering whether conduct of this sort is having an anti-competitive effect on farmers. If we determine that such is the case, we can and will seek appropriate relief under the antitrust laws.

Finally, the Division has taken two additional steps to assure that it is receiving the information necessary to make the best informed judgments with respect to agricultural antitrust issues. Last year, as some of you have already noted, the Division and the Federal Trade Commission entered into a memorandum of understanding with the Department of Agriculture to assure that the agencies would continue to work together and exchange information relating to competitive developments in the agricultural marketplace. USDA has provided us with substantial information and assistance in the past and we look forward to a continuation of that good relationship.

Of course, the Antitrust Division also works with other relevant Federal agencies on specific matters of common interest. For example, in the Cargill-Continental transaction, we worked very closely with the Commodities Futures Trading Commission because of certain aspects of that transaction that we thought might adversely impact the futures markets.

Second, earlier this year, Assistant Attorney General. Joel Klein appointed Doug Ross as Special Counsel for Agriculture. This is a newly-created position that reports directly to the Assistant Attorney General. The Special Counsel works exclusively on agricultural issues. Mr. Ross has over 25-years of law enforcement experience, both in and outside of the Antitrust Division, and has already begun to meet and speak with farm groups both here in Washington and in farm States. One of his particular qualifications is that he has a long-time relationship with the National Association of Attorneys General, and his relationship with them ensures that we will continue to have a good working relationship with the States in this vital sector of our economy.

In conclusion, Mr. Chairman and other members of the Committee, the Antitrust Division understands the concerns that have been expressed today and previously about competition in agricultural markets. We take very seriously our responsibility to assure that the antitrust laws are appropriately applied. We believe that

our record of antitrust enforcement in this important sector of the economy demonstrates our effort to fulfill that commitment.

Thank you for your time and attention. I would be happy to respond to whatever questions the Committee may have.

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

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

As you will recall, when the Assistant Attorney General, Joel Klein, was before the Committee earlier this year, he was asked whether the Department of Justice needed new laws to protect farmers and Mr. Klein responded that Justice does have the tools to address concentration. The question is using them properly. Is it your testimony today, and I gather it is from the summary of actions which you have taken, that new laws are not required, that the Justice Department is active?

I do not want to phrase your answer for you, but at the same time, if that is not the case, what do you have to say with regard to a number of suggestions of legislation that have been proposed by Senators, and they have described the details of those in your presence? There is an obvious feeling that something more is required, including more intrusion by the Department of Agriculture as a part of this entire antitrust activity.

Mr. NANNES. Senator, let me try to address both aspects of that question. Certainly, as a general proposition, we believe that the antitrust laws are the appropriate laws by which expression is given to the public policies of this country favoring competition. I know that in various eras and at other times, there may have been a question about the resolve of the antitrust enforcement agencies to enforce those laws fully and vigorously. We believe that the record, certainly in the last 17 months in particular, in the matters that I have described to you today, is a demonstration of this administration's commitment to full and vigorous enforcement of the antitrust laws.

With respect to the specific questions that have been raised about the pending legislative proposals, the administration is carefully reviewing those proposals right now, almost literally as we speak, and has not developed a formal position with respect to them. So I am not in a position where I can comment on the specifics of those proposals, but I certainly can assure you that based on the comments that I have heard here today, I will be able to relay to the people who are doing that review, and I expect to be participating in it myself, the specific concerns and the proffered solutions that have been tendered.

The CHAIRMAN. I know all Senators will appreciate your conveying the gist of the hearing toady, and, in fact, the actual record as it is produced, to your colleagues. Likewise, we would appreciate your formal comments, or the formal comments of the group that is considering these bills, so that we can make that available to all members of the Committee and the staff. Obviously, that question will be raised with you and other witnesses throughout the hearing. So if, in fact, you are in study, obviously you do not have the formal comments, but we ask for you to proceed with that as rapidly as you can so that we can continue with our business.

Mr. NANNES. Yes, Sir. We certainly understand the importance of the issue to you and other members of the Committee and will endeavor to move forward promptly.

The CHAIRMAN. Last November, the distinguished Ranking Member, Senator Harkin, and I introduced legislation to create a position within the Antitrust Division of the Department of Justice to enforce U.S. antitrust laws with respect to the food and agricultural sector. In fact, as you have pointed out, Mr. Klein has appointed Mr. Ross to take on these activities.

Let me ask two parts to the question. First of all, how far along has Mr. Ross progressed in his work? Has he seized the issues and what is he doing? This is a question that was raised really 3-months ago and we are still curious about it.

And second, should this special counsel position that Senator Harkin and I were advocating be made permanent and subject to Senate confirmation? Is the creation of the position worthwhile? Is it okay with regard to the way that it has been handled or should we have a more permanent, formal status for this position?

Mr. NANNES. Senator, I think we are very pleased, not only with the position as it has evolved but with Mr. Ross as the person to fill that position for the first time. I have known Doug now going back almost 20-years and was directly involved in our decision to appoint him to that post.

I think the post is working out very well for a number of different reasons. First, it is just very helpful to have someone who is focusing exclusively on a particularly important segment of our economy. Doug spends full time on agricultural antitrust issues, so there are no other issues competing for his attention.

Second, he is available and has met with a number of farm groups here. He has been also out on the road. I think he has met with the staffs of a number of members of this committee, so that people are beginning to understand that he is a particular focal point for people with concerns about agricultural issues. In many respects, as you know, as an enforcement agency, we are dependent upon people bringing to our attention circumstances in which they believe there may be violations of the antitrust laws occurring. So it is very important for us to, in essence, get the word out that we are anxious to have that information brought to our attention and there is someone paying attention to that on a full-time basis.

Substantively, Doug has participated in a number of activities with the U.S. Department of Agriculture. He brought some experience generally in the field to him when he arrived in January, and so I think he is very much up to speed and doing very well.

With respect to the position, it is not a political position, it is a career position. It is one that we would have every expectation would be continued, and we think at its present level and in its present form it is doing what you and others hoped that it would.

The CHAIRMAN. Senator Harkin.

Senator HARKIN. Thank you very much, Mr. Chairman.

I must say, I was reading ahead. I had read last night and I wanted to go over it again, the testimony that will be given on the next panel by Professor Carstensen of the University of Wisconsin, because a lot of the things he was saying in his testimony—I hope

you will read it, Mr. Nannes. I hope you will get his testimony and take a look at it. I do not know if you can stick around for it.

While on the one hand I applaud the Department of Justice for being more proactive in the area of antitrust enforcement overall, witness the Microsoft case, and in agriculture in specifics, looking at Continental and Cargill and the other ones that you mentioned in your testimony, I must also say that I am somewhat concerned about the narrow focus of the antitrust actions that are being taken.

You said in your testimony, at the beginning, if I can find it here again, that the antitrust laws prohibit the acquisition of stock or assets if "the effect of such acquisition may be substantially to lessen competition or to tend to create a monopoly." This enables us to arrest anti-competitive mergers in their incipiency, etc., etc., and on and on.

With regard to the Continental-Cargill merger, Mr. Carstensen points out a couple of things. First of all, he pointed out in the beef packing industry, he said that, as Senator Conrad, I think, was pointing out and has always pointed out, the four largest firms control 78-percent of the slaughter. But there were 22-plants with the highest level of production accounting for 80-percent of all production. Okay, you understand there were the four largest firms that controlled 78-percent of the slaughter, but there were 22-plants under that, that did 80-percent of the production. Assuming that such plants reflected the greatest scale economies and operations, achieving such scale economies would require less than 3.7-percent of the market.

Do you see how he figured that, 22-plants, 80-percent, 3.7. In pork, the 31 largest plants yield 88-percent of the production, which means that each plant requires less than three percent of the market, yet they are all owned by a few people. But each plant on economies of scale are doing less than three percent.

OK. Then I want to leap from that to the Continental-Cargill merger. The government, as Mr. Carstensen—I am just going to read from his testimony because it reflects my concerns. The government insisted only on isolated divestitures—you mentioned those—isolated divestitures where it identified specific quantitatively substantial overlaps between the merging firms, *i.e.*, the Coast elevators, a few elevators on the Coast, one on the Mississippi, that type of thing. In many instances, including key export facilities, not surprisingly, the prospective buyer of those assets is another of the few major global grain traders.

Thus, global market leaders are cannibalizing a third firm. The Antitrust Division in its justification for the settlement recognized that pervasive competition between Cargill and Continental, but its proposed relief ignored the overall operation of grain trading in which large integrated firms have come to dominate it. By allowing the dismemberment of one of the leaders, the Government has effectively reduced the number of real competitors in a significant way. This is a failure to consider the overall context because of blinders, of a theory of competitive effect that ignores the larger and longer-run implications of these complications.

Well, that sort of gets to the heart of my problem with some of this. Sure, you go in and you say, well, okay, you can go ahead and

merge, Continental and Cargill. You can go ahead and do that, but we are going to pick off a few of these elevators here and there, and who buys them? Another large grain trading company. It does not mean a darn thing. I do not think it is going to mean one lick of difference to my farmers in Iowa whether or not those elevators are owned by Continental-Cargill or Bunge or one of the other large trading companies. It is not going to mean a thing.

It would mean something, however, if they were, in fact, divested and not put out to be picked up by another global company, but were, in fact, put on the market to be picked up by smaller entrepreneurs out there who could effectively bid in an open and competitive way for grain. Do you understand my point?

Mr. NANNES. I do, Sir.

Senator HARKIN. Well, I guess, then, my question is, is the Justice Department looking at the broader overall implications of this rather than just going at a few isolated little grain elevators, saying, well, if Continental owns an elevator in East Dubuque and so does Cargill and they combine, then there is nobody else there. We have got to make them divest of that. But if it is picked up by Bunge, where does that leave my farmers?

Mr. NANNES. Senator, let me tell you what we did in that case, because I think if you understand the process that we went through, you may take greater comfort from the fact that even though the relief that we ultimately sought has been characterized as individualized, in fact, it represents the areas of competitive concern that we identified.

We did a very comprehensive review of Cargill-Continental. We literally looked at every facility that Continental was selling to Cargill and plotted on maps the proximity of facilities to one another and then ascertained what farmers were, as a practical matter, dependent upon those facilities, and if farmers were dependent on those facilities, we looked to see the other options to which farmers could turn if the operator of the Cargill-Continental facility sought to depress price arbitrarily. And where we believed that the number of options would be diminished substantially to farmers, we sought relief.

Now, in a couple of the instances, what we wound up getting were divestitures of, say, river elevator facilities. But in other instances, we got divestitures of port facilities, and in particular, with respect to the relief we got in the Pacific Northwest, that was based on our assessment of actual patterns of travel and traffic because of farmers in the Dakotas who were, as a practical matter, dependent during most seasons of the year on access to a competitive port structure in the Pacific Northwest in order to get a fair price for their grain and their soybeans.

So we did look at it very broadly and we looked at it very thoroughly, and it may be that in this particular case, the nature of the relief that we sought and were able to obtain has to be defined ultimately in terms of the specific facilities, but our focus on it was indeed very broad.

Now, we also have the authority under our final judgments that are entered in these matters to determine in our unilateral discretion whether the proposed purchaser of a divested facility is a purchaser that we regard as pro-competitive or anti competitive. So if

we have circumstances where a party that proposes to make an acquisition of a divested facility in fact intensifies or complicates or exacerbates the competitive situation, then we have the right to just say no, and we have in various cases over time rejected proposed purchasers because of the concerns that you articulated, that it is simply substituting one fox for another fox in the chicken coop. So we take those very much into consideration and we try to review it broadly enough to understand what is the essence of the transaction we are reviewing.

Senator HARKIN. Would you provide for the Committee who some of the prospective purchasers of these port facilities and elevators are?

Mr. NANNES. We will be happy to provide the Committee with information about the case, Sir.

Senator HARKIN. I do not know the answer to that. I would just like to know if there are other prospective buyers out there, if there are different buyers out there that do represent a competitive force. I do not know if you are allowed to do that. Can you supply that to us or not?

Mr. NANNES. We will endeavor to do so, Sir.

Senator HARKIN. I do not know if that is allowed or not, but if it is.

The second part of my question has to do with, we are talking about all these horizontal mergers, but another thing that is affecting us is the vertical integration, and I want to know, again, what your authority is. I am not really clear. I have looked at the law. I have tried to understand this. But what is your authority under vertical?

We just had last fall Smithfield, the largest pork packer, bought Murphy Farms, which is the largest pork producer. So again, I think that seems to me to be some kind of a vertical. You have got the producer and then you have got the packer.

As I understand it, the Antitrust Division and FTC give a lot less attention to vertical alignments, but I think this Smithfield–Murphy combination, merger, acquisition, I guess it is called—I do not know what it is called—may have had a more massive effect on the competitive element in the pork industry than any other kind of horizontal thing that could have happened, and yet, what have you done about it? I mean, as far as I see, nothing is happening on the Smithfield–Murphy acquisition, vertical alignment.

Mr. NANNES. Senator, let me try to respond to your question this way. Certainly, the antitrust laws do allow us to take a look at the competitive implications of transactions that are basically vertical in nature, where firms at different levels in the production or marketing process are aligning. And indeed, we do so.

It is probably fair to say that, more so than with respect to horizontal transactions, the vertical transactions also have significant pro competitive features. If you take it out of the agricultural context for a second and just consider the matter more broadly, there are circumstances in which a manufacturer by acquiring an input supplier gets a more certain, regular supply of inputs. It can tailor the inputs to fit more efficiently into the manufacturing process that it pursues, so that vertical transactions often have pro competitive features which are, indeed, what motivates them.

Now, there certainly can be circumstances in which vertical acquisitions can be competitively problematic. If the result of a vertical acquisition is to create competitive problems at either level of the transaction of a sort that is going to diminish ultimate supply by foreclosing people from the market, then, indeed, there can well be circumstances in which there would be a proper case for antitrust intervention.

Senator HARKIN. My question was Smithfield-Murphy. Are you doing anything on it?

Mr. NANNES. Smithfield-Murphy was a transaction that we looked at very carefully, in part because the companies were large relative to other participants in their lines of business, even though they did not have particularly high market shares in either of those lines of business. We talked to a number of persons potentially affected by that transaction in the markets where the companies operated, and by and large, Sir, we were told that people there were not concerned.

Senator HARKIN. Who? What people were not? You did not talk to any of my hog farmers.

Mr. NANNES. We would talk to farm groups who either had—farm interests who either had sold hogs to Smithfield or were looking to buy and assure that there would be a source of supply for their processing plants, and what we were told was, generally, they believed that they had sufficient alternatives to which they could turn so that they were not concerned about the competitive implications of this particular transaction.

Senator HARKIN. I do not know. I do not find that response very responsive. There are a lot of independent producers out there who are going to be drastically affected by what happened with Smithfield and Murphy. They are already being affected by it. You say you contacted farm groups and people like that, but, I mean, is this just sort of a weighing thing? You sort of look at it and you sort of say, well, we sort of asked a few people. I mean, the law is the law. I just read to you what you said here, that you have—if the effect of such acquisition may be substantially to lessen competition or tend to create a monopoly. If Smithfield and Murphy does not do that, and I do not know what does.

And I am sorry, there are independent producers out there that are going to be drastically affected by this Smithfield-Murphy because they are going to lock up the contracts. You are not going to have a lot of producers or even processors out there, small processors, that will be able to compete against this. And yet you are telling me that you talked to a few farm groups and they said it was okay? That is what I heard. Maybe I did not hear it right.

Mr. NANNES. Senator, here is what we do. If we have a situation where we are looking at a proposed merger, we try to ascertain the impact that the merger is going to have in the particular markets where the companies operate. I know as a general matter there is an apprehension and a concern about the trend toward vertical integration, but when it comes time to look at whether we can enjoin a transaction for violating the antitrust laws, we have to develop evidence based on the likely impact of the transaction in the markets where the companies operate, and we endeavor on those occasions to reach out to potentially affected persons.

When we do merger reviews, for example, we get information generally about customers in the geographic area so we can reach out to the customers. We can reach out to State officials. We can consult with the U.S. Department of Agriculture to try to get a handle on what the impact of a particular transaction is likely to be.

Senator HARKIN. I did not hear one word that you just mentioned about pork producers, about hog farmers. You talked about customers, the people that may be buying from Smithfield and Murphy, but how about the people that are selling to them?

Mr. NANNES. In the context of a particular transaction, such as Smithfield-Murphy, the people with whom we were speaking were farmers.

Senator HARKIN. And you are saying that the farmers you spoke to just seemed to think this was just fine?

Mr. NANNES. They were not concerned that as a result of this transaction they would be unable to get their hogs to processors.

Senator HARKIN. Well, I will ask the Iowa Pork Producers and I will ask some more pork farmers. That is not what I am hearing, but I do not know. I find that just amazing to me. But we will ask the pork producers and see if they think this is a good deal for their pork farmers.

Thank you very much, Mr. Chairman.

The CHAIRMAN. I thank the Senator.

Senator Grassley.

Senator GRASSLEY. Thank you, Mr. Chairman.

I want to say something and then I have got kind of an unrelated question that I want to ask, unrelated to my remarks. What I am saying is meant to supplement what Senator Harkin said and not detract from it.

First of all, in the abstract, hearing about the evidence of challenges that you have made and things of that nature, I think would be impressive in isolation, but maybe in the overall concern that farmers in my State have about concentration, it does not seem like much because, quite frankly, things have been worked out and settled and there has not been very dramatic impact made of just exactly what is a guideline of response to the concern for the mergers that have been presented to us as members of Congress.

Now, again, to emphasize, not to detract from what Senator Harkin said, I think when I introduce legislation as I have described it, I have to be somewhat appreciative of Assistant Attorney General Klein, other people that work for him, about their listening to our concerns and attempting to respond to our concerns, and I think you have attempted to give some good evidence of that, and in both public and private conversations, I think I sense within your Department the concerns that you are trying to present to us here today. I do not think, though, at the grassroots of America that they would be seen as being enough, and maybe you could say, well, that is the usual criticism of "what have you done for me lately" that maybe we get hit with too often as political leaders or even as administrators, as you might get.

But I do want to acknowledge that I think there has been a good faith effort by your Department to take into concerns, and I am not sure that I felt that before we started expressing those. Now, there

may have been an understanding, and hence, then, my legislation, and probably to some degree the legislation that others have put in, although maybe the other legislation does not impact upon the Department of Justice as mine does in the sense that the Department of Agriculture has kind of a shotgun behind the door that it can use in case that there is some disagreement with whether or not the Department of Justice has done enough to take the position of the family farmer into concern.

So I just say those things, maybe a little bit apologetic about introducing a bill that you might see as an outright statement of resentment that the Department of Justice has not done enough at the same time when I have probably told some of you privately that I appreciate some of the things you have done. At least you are listening to our concerns and responding to them, and I guess to some extent the Cargill-Continental arrangement is part of that.

But let me suggest to you that the bill should not be seen—my legislation should not be seen as doing anything more than supplementing a case that you have tried to make here that the Justice Department is taking our concerns to heart and have acted upon those. I think the extension is that I would see the Department of Justice more at the table in a more specific way than your memorandum of understanding would have it, and then have the ultimate power if the Justice Department saw fit not to challenge a merger, of the Department of Agriculture doing that on their own under a separate standard than as what is in the present antitrust laws.

I have tried not to deal with the antitrust laws in a direct way because I think we have had evidence from people both in the Justice Department and people outside the Justice Department, including my own distinguished professor Neil Haral at Iowa State University, who said that the antitrust laws did not need to be changed. But giving a role to the Department of Agriculture more specific with the Justice Department and then a separate role as kind of a shotgun behind the door approach. Now, I have said that all to caution you that I am not out just to find fault with the Department of Justice.

Now, a question a little bit unrelated to what I have just said, and only one question, when the Department of Justice has concerns about a merger, how often, and maybe a general statement but maybe with some sort of quantifiable response, how often are you able to work out those concerns with the merging parties without litigation?

Mr. NANNES. That is a fair question, Senator. Generally speaking, if we are able to work out our issues with parties, that workout can occur one of two ways. We conduct our investigation and assume that we come upon a transaction that we believe is competitively problematic. We will identify our areas of concern for the parties and give them opportunity to try to address them. Sometimes they address them, in a sense voluntarily, by restructuring the transaction and divesting the asset before we complete our investigation, in which case there may not be even an occasion for us to sue them.

On the other hand, it more generally happens that they agree to make certain divestitures as a condition of proceeding with the deal

and then we will file a complaint and there will be a competitive impact statement and a final judgment and the decree will embody the relief to which the parties have agreed at our insistence.

Alternatively, there are situations where we believe that a transaction simply cannot be restructured, that the competitive problems with it are so deep that they cannot reasonably be remedied. There are occasions, then, when a party will simply voluntarily abandon the transaction and not force us to file a lawsuit, and so there are circumstances where I talk about merger challenges where you will not find that we filed the case because we advised somebody of our intent to sue and they said in those circumstances they would simply not go forward. But where, in fact, they are not prepared to abandon the transaction, then we have to litigate.

Of the total number of cases that we find to be competitively problematic, the vast majority of them, probably well over 90-percent, are resolved through final judgments and restructurings that are negotiated between us and the parties, and a much smaller number of those actually go through the litigation process. But when we do settle with them, we have to file that settlement with the court, and as I think many of you know, under the Tunney Act, the district court then reviews the settlement to determine whether it is in the public interest.

Senator GRASSLEY. Thank you, Mr. Nannes, and I am done.

The CHAIRMAN. Senator Baucus.

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

Senator BAUCUS. Thank you, Mr. Chairman.

Mr. Secretary, I just would like to change gears here to go into deeper thoughts as a consequence of globalization and advances in technologies. It is clear that the United States economy is doing well in part because there is more mobility, opportunity, and competition. There is a little less regulation and more of a culture and atmosphere of individuals attempting to pursue and new opportunities and increase their incomes.

We have now come into something called the new economy. I am not sure what that is, but it has something to do with high tech and the Internet. Where our new opportunities are tremendous and where the rewards often go to the most educated or the more highly skilled Now, we cannot turn the clock back. We can only go forward. That is, we cannot go back to the horse and buggy days, and nobody would argue on that. Times do change. Technologies change. Competition changes.

We all know that the free market is a very powerful engine. It has done a lot for America and a lot of people. We also know that this free market has its limits. That is, when people pursue a free market philosophy, they buy, sell, merge, and acquire. That is the American way. But often, or at least sometimes, it has a pernicious effect on others. People talk about the digital divide and people also, I think, note there is now, as a consequence of globalism, an economic divide.

The basic question is, how do we deal with this situation? We have the Sherman antitrust laws and the Department of Justice is, pursuant to them, pursuing Microsoft. They think Microsoft is mo-

nopolistic, and anti-competitive in a certain sense. That is the view of the Justice Department.

So my question concerns your thoughts in general on how we draw the line, concerning antitrust issues. Without getting too much into horizontal and vertical and too much into the intricacies of antitrust law, but just generally, because, after all, we are all here to try to figure out how to best arrange ourselves as a society and times are changing so quickly. We certainly want to protect shareholder value, protect investors. There are provisions in corporate law which require that. Maybe corporate law needs to be changed, I do not know. I am curious.

Mr. NANNES. Senator, I———

Senator BAUCUS. Clearly, in the subject of this hearing, there are a lot of farmers and a lot of livestock producers who are really hurting as a consequence of all this, of globalization and mergers and concentration, whether it is the packing industry or in the retail industry or what not, and there is not a doggone thing they can do. That is about it in most cases. They are just stuck. They are falling farther and farther behind.

Now, one can say in some other industries, say in telecommunications, that when market forces cause changes, well, you can always either merge or be acquired or do something, and generally your income does not fall. Your ego may be bruised, but your income does not fall. That is not true in agriculture for the most part.

How far should the free market go in driving farmers and ranchers out of business? Do you feel that the line should be drawn somewhere so that the average farmer or rancher is not wiped out? Where do you drawn the line to prevent that and how far do you prevent it?

Mr. NANNES. Senator, generally speaking———

Senator BAUCUS. If you could wave the magic wand, forgetting all our laws, if you could say, I am king for a day where would you draw the line?

Mr. NANNES. It is difficult to know exactly where to begin to get into that arena, Senator. Stepping back very far and looking broadly at world trends, I think I believe, and I know Mr. Klein believes that the direction favors the American way. To the extent that, over time, there has been a competition between having open economies and controlled economies, differences as to whether private people ought to be able to make the decisions about the lines of business they pursue or whether government is going to tell them what they can or cannot do, it appears now that the American way has prevailed over the controlled economy way.

And generally speaking, part of our current prosperity is probably attributable to the fact that we have been a leader along that paradigm and an increasingly large portion of the world seems to be concluding that, that is the direction and the way to go.

A corollary of that is less direct government intervention, but it is important that something fill the void to make sure that these free-market decisions that are being made by people are not being done in a collusive or otherwise anti competitive way that are, in fact, expropriating to private parties the gains that should flow to the economy as a whole.

So it seems to us that appropriate antitrust enforcement is the key to an open market economy, because if antitrust laws are not appropriately enforced and citizens of a country or the world conclude over time that they are being abused by private anti competitive conduct, they will turn, as people have at various stages of our history, back to the Government and ask for there to be direct regulatory controls imposed as the way of reigning in those excesses.

So those of us who champion the free market system, I think, have a similar obligation to champion appropriately aggressive antitrust enforcement to prevent excesses of the market from overwhelming what otherwise ought to be a freely competitive process that best allocates resources, that leads to more innovation, and that results ultimately in appropriate prices.

Senator BAUCUS. I understand that, but in all due respect, you did not answer the question. You stated general principles. Where do you draw the line?

Mr. NANNES. Well, I think the line is appropriately drawn if antitrust laws are appropriately enforced. I think that is the appropriate line. Our antitrust laws in this country have stood the test of time.

Senator BAUCUS. Do you think they are appropriately enforced today with respect to this issue?

Mr. NANNES. I think they are appropriately enforced today.

Senator BAUCUS. Which is to say they are basically not enforced, or there is no action taken?

Mr. NANNES. I do not agree with the perspective that they are not being adequately enforced. What I think is going on here———

Senator BAUCUS. What actions are being taken pursuant to American antitrust laws to address concentration by the Department?

Mr. NANNES. The most direct way in which the antitrust laws address concentration is by preventing its accumulation through a merger, and we have a very aggressive merger enforcement program. But one of the ways, it seems to me, to respond to some of the concerns that you have expressed about family farmers—and I do not presume to say I know them anywhere near as well as you do, but I have met with enough farmers and farm groups to know that the pain you articulated on their behalf is real and genuine—is that there has to be an array of policy responses to address the concerns that farmers currently have.

Senator BAUCUS. What is this thing called oligopoly I remember reading about when I was in college taking economics courses? Does that apply here?

Mr. NANNES. Well, you certainly have some industries that are highly concentrated and that is generally associated with an oligopoly structure, and there are circumstances in an oligopoly structure in which companies can act anti competitively. But under our antitrust———

Senator BAUCUS. Why today is the oligopolic structure of the concentration of the beef-packing industry not actionable?

Mr. NANNES. Well, under the antitrust laws, unless we have a situation where a single company has a monopoly, companies are generally free to set their own prices.

Senator BAUCUS. What about oligopolies? We are talking about oligopolies, not monopolies.

Mr. NANNES. I understand, but the point I am getting to is that on those occasions where we have cause to believe that companies in an oligopolistic industry are explicitly or impliedly agreeing upon price and terms and other conditions of doing business, we can and have sued them under the antitrust laws. Indeed, we will prosecute them criminally.

Senator BAUCUS. To what degree does the Department look to see whether there is implicit, indirect implicit, not explicit, but implicit or indirect, if not collusion, at least coordination?

Mr. NANNES. Well, under the antitrust laws, the Sherman Act, we have to be able to prove that there is an agreement.

Senator BAUCUS. That is not the question I asked. It has to be an agreement.

Mr. NANNES. I am trying to get to the point to tell you that to prosecute under the antitrust laws, we have to be able to prove an agreement.

Senator BAUCUS. OK.

Mr. NANNES. Now, the question is, how do you get proof of that agreement, and you can get proof of that agreement, as we do often in price fixing cases, by getting someone to come forward to the Government because they believe they have observed unlawful behavior and give us a key to get in the door to uncover———

Senator BAUCUS. We are not talking about explicit agreements here. We are talking about implicit coordination. Is that not actionable?

Mr. NANNES. The antitrust laws draw a very clear distinction between two different propositions, so if you do not mind, let me set them out. If you have a situation where one company is setting its own prices or its output or its marketing decisions based upon its perception of what its competitors are going to do in response to conduct that it may take, that, in a sense, is interdependent behavior because they are looking at what to expect from the competitor and taking that into account before they act. But that would not ordinarily be regarded as an agreement which would be actionable under the antitrust laws.

If instead they are communicating directly with one another, or even indirectly through intermediaries with respect to that kind of business behavior, then we may have the basis for finding that there is an agreement that is prosecutable under the antitrust laws.

Senator BAUCUS. Do you think laws are needed?

Mr. NANNES. I think that distinction is an appropriate distinction. I think there would be enormous difficulties in a regime that tried to prohibit one company from taking into account its competitor's likely responses in deciding what it was going to do.

Senator BAUCUS. What if it is clear that they are all working together, they kind of know what each other is doing and it is kind of a wink and a nod situation?

Mr. NANNES. There are some cases that teeter on one side of that line or the other. We are aggressive in trying to ascertain the essence of what is really going on in those circumstances. If we find

a basis for believing that an agreement is what explains their behavior, then we will move very aggressively with respect to that.

Senator BAUCUS. Another aspect of this is just a lot of these outfits requiring competitors overseas. I am not very knowledgeable on what I am about to say, but I would not be surprised if, say, Brazil, for example, a huge potential increase in beef exports from Brazil to the United States in the next several years, and I have got a strong suspicion that a lot of American companies, the two or three, the ones we all know we are talking about, have acquired or have interests in Brazil and in other countries, Australia, for example, and that just has, again, more anti-competitive effect, or it tends to have the effect of blocking out the producer.

Have you spent much time on a farm or ranch?

Mr. NANNES. I have not.

Senator BAUCUS. I think you should.

Mr. NANNES. I would like to.

Senator BAUCUS. Is there any department that really knows much about this, about farming or ranching?

Mr. NANNES. We work extremely closely with the U.S. Department of Agriculture, and so———

Senator BAUCUS. You know a lot about the high-tech industry.

Mr. NANNES. I am sorry, Sir?

Senator BAUCUS. You know a lot about the software industry and operating systems.

Mr. NANNES. That is correct, Sir. I mean, we have to become fully informed and advised with respect to any transaction that we are reviewing.

Senator BAUCUS. How much time has the Department spent looking into this question, this concentration in the beef-packing industry? How much time has the Department spent looking at it?

Mr. NANNES. I do not know specifically with respect to the beef industry. I think we recently responded to a letter that the Chairman had sent us trying to detail for him the people who work in the Division on a regular basis on agricultural matters.

Senator BAUCUS. So you do not know? You do not know how much time the Department has looked into this?

Mr. NANNES. Senator, I can tell you that with respect to a particular transaction, we devote not insubstantial time to examining the industry that is involved in the transaction.

Senator BAUCUS. Mr. Chairman, there is clearly a problem here and it is clear that nobody has come up with the right solution that I am aware of. I am on legislation that tries to get at this problem, and I think anybody who knows much about this subject knows that there is a problem, and I am a little bit distressed, frankly, that the Department does not seem to be undertaking efforts commensurate with the problem to try to solve it.

I do not know why, but my sense is, just talking to you and what is going on around here, the Department is not and I very much hope that it does, because you are there to serve farmers and ranchers just as much as you are there to serve the American public on the Internet and who buys computers. That is your job, right?

Mr. NANNES. Yes, Sir.

Senator BAUCUS. Are you going to be spending more time?

Mr. NANNES. Senator, we spend very substantial resources and time on agricultural antitrust issues.

Senator BAUCUS. It does not sound like it if you do not know what you are doing. You just said—I do not mean to badger you. Just a few minutes ago, you said you do not know how much time and effort the Department is spending on this.

Mr. NANNES. Senator, I cannot quantify it for you. That is different in implication and import from suggesting that we do not spend substantial time on agricultural matters.

Senator BAUCUS. Well, if you do not know, I have a hard time concluding that you are spending a substantial amount of time.

My time is up, Mr. Chairman. Thank you.

The CHAIRMAN. Thank you very much.

Senator Fitzgerald

Senator FITZGERALD. Thank you, Mr. Chairman.

I want to focus a little bit specifically on the two bills the Committee is considering, Senator Daschle's bill and Senator Grassley's bill, and I am wondering, you have said that the DOJ does currently consult with the USDA and you have talked about spending a lot of time with farmers and farm groups, and I am wondering, do you have a formal process inside the DOJ to consult with the USDA on agricultural mergers?

Mr. NANNES. Yes, Senator. We have a memorandum of understanding with the Department of Agriculture that provides a framework within which we will consult one another with respect to agricultural issues with competitive implications. If we are reviewing a merger of some significance with respect to the agricultural sector of the economy, it would be a regular process for us to reach out to the U.S. Department of Agriculture, although frankly, if the truth be told, they often reach out to us first and we have opportunities to share thoughts, concerns, theories, sources of information, sometimes even information itself.

Senator FITZGERALD. Would these two bills, would either of them change your relationship with the USDA, then? I do not know if you have looked at the bills specifically, but how would they change how you currently work with the USDA?

Mr. NANNES. Senator, you are correct that I have not reviewed the bills line item by line item, and that is something that we will be doing in the near term through the administration process of developing a position with respect to the bills. We have cooperated with the Department of Agriculture in the past, and I would expect that no matter what happens, we would continue to cooperate with them in the future because they provide us with valuable input as we hope we provide them, as well.

Senator FITZGERALD. Will you eventually be coming out with an official position on these bills?

Mr. NANNES. It would be my expectation that we would, because I understand we have been asked for one, Sir.

Senator FITZGERALD. OK. One final question. I guess opponents of both of these bills argue that providing the Hart-Scott-Rodino filing information to the USDA would potentially jeopardize confidentiality of proprietary information. Do you see this as a problem or do you already share this information with the USDA Secretary?

Mr. NANNES. No. At the present time, Sir, under the Hart-Scott-Rodino statute, the information that we receive must be treated confidentially within the antitrust enforcement agency. Over time, we think that has worked extremely well because companies provide us with information that is extraordinarily sensitive from a competitive point of view and they often contrast what they do with us with what they have to do in other regulatory proceedings, where sometimes information that they submit becomes available to their competitors and thus has a counterproductive impact.

Senator FITZGERALD. But there are areas where this information is shared. Say if there is a banking merger, the Federal Reserve is in on the information, I would imagine, along with potentially the DOJ.

Mr. NANNES. I think what generally happens there is that the confidentiality restrictions that apply to Hart-Scott-Rodino apply even in those circumstances, though it may be that in those particular banking instances to which you refer the parties are submitting different information to the banking agencies.

Senator FITZGERALD. OK. Thank you very much for your time.

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

Mr. Nannes, we thank you for your testimony, for being very forthcoming in your responses. The Chair has had a liberal policy with regard to Senators' questions because clearly the antitrust issues that you are dealing with are at the heart of the legislative proposals that many Senators have made and the questions that the Committee has been raising in these four hearings we have had on consolidation. We thank you for working closely in your answers with the Senators and their questions.

Mr. NANNES. Thank you, Senator.

The CHAIRMAN. The Chair would like to call now a panel composed of Mr. James Rill with Howrey, Simon, Arnold, and White. Attorneys at Law, of Washington, DC.; Mr. David Nelson, Director of the Equities Division, CS First Boston, New York, New York; Mr. Peter Carstensen, Professor of Law at the University of Wisconsin Law School in Madison, Wisconsin; and Dr. Stephen Koontz of the Department of Agriculture and Resource Economics, Colorado State University in Fort Collins, Colorado.

Gentlemen, I ask you if you can to summarize your statements. They will all be made a part of the record in full. We will ask that you summarize in as close to 5-minutes as possible, but within 10-minutes as absolute, and then this will offer opportunities for Senators to raise questions of you.

Mr. Rill.

STATEMENT OF JAMES F. RILL, HOWREY SIMON ARNOLD & WHITE, ATTORNEYS AT LAW, WASHINGTON, DC.

Mr. RILL. Thank you, Mr. Chairman, Senator Grassley. My name is Jim Rill and I am testifying today on behalf of an industry structure coalition, a large number of food and agricultural trade associations and groups which oppose S. 2252 and S. 2411. The identity of these groups is listed in my prepared statement, which you kindly indicated will be made part of the public record.

I want to focus my testimony today on the portions of this legislation dealing with mergers and acquisitions in the agricultural

arena. The proposed legislation would give the Department of Agriculture overlapping authority with the antitrust enforcement agencies, the Department of Justice and the Federal Trade Commission, to review and challenge competition-related aspects of certain mergers and acquisitions in the agribusiness industry.

During my, I hate to admit it, more than 40-years of practicing antitrust law, and more recently in my capacity as co-chair of the International Competition Policy Advisory Committee, appointed to that role by Attorney General Reno and Assistant Attorney General Klein, I have had the opportunity to witness firsthand and review the competition aspects of mergers involving a variety of agencies.

As a general matter, dual jurisdiction, jurisdiction of the general enforcement agencies and of the sectoral agencies, to challenge mergers on competition grounds is costly and undesirable for several reasons which I want to discuss. The issue of overlapping jurisdiction was one of the issues addressed by the International Competition Policy Advisory Committee [ICPAC], which I will refer to as ICPAC, if I may.

We were appointed to provide recommendations on the future direction of international antitrust policy within the framework of evolving markets and rapidly increasing globalization. In the final report issued on February 28, the majority of the Committee concluded that the oversight authority for competition-related aspects of merger review should be removed from sectoral agencies, such as the FCC and the Surface Transportation Board. This conclusion was based on the belief that overlapping jurisdiction is costly for both business and the enforcement agencies, promotes a lack of transparency and consistency in the enforcement process and possibly in the enforcement result, and may produce results that deviate from widely accepted standards of competition policy, consumer welfare, and welfare for the economy in general.

Under the ICPAC recommendations, however, sectoral agencies would retain the authority over all non-competition-related aspects of merger review as they may be authorized to do so by statute, for example, the effect of a telecommunications merger on security or on universal access, which are not so much competition-related issues.

The Committee's recommendations in this regard have actually been cited favorably by some of the sectoral regulators themselves—Commissioner Powell at the FCC, Commissioner Furchtgott-Roth at the FCC, and FERC Commissioner Hebert, all of whom seem to at least be inclined favorably to consider the proposals of the ICPAC.

Over the past almost 100-year history of U.S. merger law, merger review standards have been relatively transparent, relatively well understood, and generally accepted. These standards cover most consumer welfare and the threat of monopsony power. The proposed legislation threatens to undercut this clear and articulated approach and impose new competition standards on mergers in the agribusiness industry and authorize the USDA to impose challenges based on these standards.

These standards may or may not be consistent with antitrust-based standards as articulated in the Clayton Act, and at the very least, I think we would have to agree, not supported by the coral

reefs of litigation that have developed standards under the Clayton Act. Such standards would be ambiguous and would add time and cost and uncertainty to their implementation.

In view of the yellow light, I do not want to get into any great detail to repeat the testimony that was given by Deputy Assistant Attorney General Nannes, but the fact is, when one asks how many of the resources of the Antitrust Division have been devoted to mergers and other activities in the agribusiness field, I think the record of challenges to four mergers in a relatively short time period, the record of criminal fines of record proportions in that same time period, would suggest that the aggressiveness and vitality of antitrust enforcement in the agribusiness field would compare—I am sure the defendants would not agree with this, but would compare favorably with the activity of the Department in any other sector of the economy.

In the Cargill-Continental grain matter alone, 20 staff individuals, staff attorneys of the Antitrust Division, I am informed, were devoted to the review and challenge and resolution of that merger proceeding. I would simply incorporate in my prepared statement these cases and also to cite the statement of Deputy Assistant Attorney General Nannes as a very strong record of Department of Justice enforcement in this area in the merger and actually in the criminal enforcement field, as well.

This testimony should not be taken as any lack of concern with the economic condition of the agricultural sector of the economy or family farmers, but based on these examples and based on our review of merger law, there does not appear to be any evidence that would suggest that mergers in the agribusiness sector have been cleared without appropriate remedies so as to restore or preserve competition. I do not think, then, the case has been made for a separate merger law to be enforced by the Department of Agriculture apart from, or in addition to, the merger law actively enforced by the U.S. Department of Justice.

Thank you, Mr. Chairman and Senator Grassley.

[The prepared statement of Mr. Rill can be found in the appendix on page 98.]

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

Mr. Nelson.

STATEMENT OF DAVID C. NELSON, DIRECTOR, EQUITIES DIVISION, CS FIRST BOSTON, NEW YORK, NEW YORK

Mr. NELSON. Thank you for inviting me here today to share my perspectives regarding some of the dynamics currently affecting agribusiness and the food industry.

First of all, from a financial perspective, performance of agribusiness companies and agribusiness stocks has been quite dismal. Since January 1997, agribusiness stocks on average are down by one-third. Farmland actually has been a better investment over that time frame. This poor agricultural stock performance has been during one of the greatest bull markets in history, where the S&P 500 has doubled over that time frame.

The key drivers here are poor returns on capital, slow and volatile earnings growth, and an implied unattractive outlook for future returns in this sector. Highlighting the obvious, stock prices reflect

investors' expectations of future returns, not necessarily current or past performance. It is clear from the voting booth of the stock market, investors are voting to disinvest in agribusiness.

Why have returns been so poor? A few thoughts. The value chain across the entire food industry is contracting. There is a power shift taking place from food companies to retailers, but also from retailers to consumers. The profit challenge being faced by farmers is not unique across the food chain. These shifts happen. Consumer needs are changing at an increasing rate. Corn movement, for instance, has gone from being export-oriented to domestic processed-oriented. So if you had a grain elevator in a position for the exports and now that movement has shifted, that elevator is now of little to no value. This is natural in our market economy of creative destruction.

Another challenging factor to food companies is what I call commotidization. The bar to acceptable quality and convenience is constantly rising. For instance, when Tyson took the breast off the chicken bone, that was value added. Then everyone else did it. The value and the margins came down. They marinated. Margins went up. Then everyone else did it and margins came down, and so on and so forth. Innovations are rapidly duplicated and the ability to capture value, even when successful, is relatively short-lived.

New competition is also presenting new challenges. Earlier, we cited new competition from soybean acreage in Brazil, new processing plants and soy processing plants in China. Also, domestically, cooperatives have been building new soy plants, new corn processing plants, and these players have different economics and different return objectives that make competition difficult for profit-oriented companies, especially those with public shareholders. Essentially, we have too many companies with too much capacity fighting for too few profits.

Why do we see consolidation and integration? Industry consolidation and integration occur really for two reasons. One, companies and individuals often need to sell their business because they are unprofitable or unviable in their current structure or configuration given that conditions in the marketplace do change quite rapidly. It is really a natural selection process at work. This is the reason why we do have the most productive and efficient food system in the world. As Darwin said, adapt or die.

The other primary reason we are seeing integration is really to meet the demands of consumers. We are hearing a lot of objections today, for instance, about packer ownership of livestock in the pork sector, but this is not because raising hogs is sexy or glamorous and something packers want to do. It is because they have to do it. The consumer today wants a quality and consistent product. You cannot do that unless you have an integrated and coordinated supply chain. I would rather, as an analyst, see these companies investing forward into further processing or branding than moving backward. They are moving backward because they have to.

I think it is important to note that not only are the customers of food manufacturers more demanding, they, too, are consolidating. The market share of the top five retailers, supermarkets, has gone from 25-percent to 40-percent in the last 4-years. Supermarkets are trying to consolidate the number of their suppliers just

like every other industry that is out there. They need big companies that have made the investment in information technology. Information technology increasingly is becoming that bar or barrier to entry across all industries, including food, and that requires a higher level of investment.

Now, these food companies are much smaller than the companies they are selling to. IBP has a market capitalization of $1.4 billion, Smithfield at $1.2, Hormel and Tyson at $2.3. In contrast, Kroger, Albertson, and Safeway are all at about $15 billion in market capital, and Wal-Mart is $264 billion. So they are selling to supermarkets that are much bigger, that can bring a lot more pressure to bear.

These are capital-intensive industries that require substantial reinvestment merely to stay in the game. For instance, IBP now plans to double their capital expenditures over the next year to $400 million, in large part on new equipment and technology for case-ready meat to become more competitive, to make beef and pork more competitive with chicken. In addition, the meat industry has invested over $300 million to comply with new food safety regulations, particularly the new Hazard analysis and critical control point [HACCP] requirements. Expenditures are also rising to meet rising environmental standards.

Now, this high degree of capital intensity is an unattractive feature to investors, those that allocate capital, and that is why meat packers like IBP and Smithfield, for instance, trade at price-to-earnings ratios, if you will, at five times versus the overall market at 27 times. It obviously reflects that capital as a whole is much more expensive for meat packers, for instance, than for industry or the market as a whole.

Let me just conclude in closing that investors can invest in any industry. When I go and visit portfolio managers, there is someone talking about Microsoft or Amazon before me and GE after me and just empirically they are investing away from agribusiness. This does not just affect agribusiness negatively, it impacts farmers. So I encourage you to think about the impacts that reflect to farmers with new controls and regulation on agribusiness.

[The prepared statement of Mr. Nelson can be found in the appendix on page 118.]

The CHAIRMAN. Thank you very much, Mr. Nelson. The Chair would acknowledge that you present, as a part of your testimony charts that indicated the S&P 500 and agribusiness, and specifically meat and processed, packaged foods. In essence, the charts show the S&P rising dramatically, as you pointed out, from the beginning of 1997 to the present, but in every instance, agribusiness or any part of it in decline during that same period of time as an illustration of, I suppose, the point that you are making. Investors have not been interested. They have evaluated all of these stocks and enterprises as not necessarily losers, but comparatively, relatively, very sad.

Mr. Carstensen.

STATEMENT OF PETER C. CARSTENSEN, YOUNG-BASCOM, PROFESSOR OF LAW, UNIVERSITY OF WISCONSIN LAW SCHOOL, MADISON, WISCONSIN

Mr. CARSTENSEN. Thank you, Mr. Chairman. It is a pleasure to be here and with such a distinguished panel of presenters. I, for the last quarter century, have been teaching and writing about economic regulation and competition policy, and before that I was actually a staff attorney at the Antitrust Division and so I have some nostalgia for my old home.

I am a generalist in terms of antitrust policy and competition issues, although I have had various encounters with the agricultural issues over the years and certainly have done a lot more in the last year or so, compliments of some of my former students who have gotten me into various efforts in the area.

I want to start off by emphasizing that the goals of antitrust extend beyond economic efficiency, especially short-run economic efficiency, and I have quoted in my presentation Senator Sherman's statement about not wanting economic kings just as we did not want political kings. I am also very fond of Justice Peckham's decision in the very first substantive antitrust case in which he recognizes the kinds of harms that the dynamics of markets bring about but warns that we should avoid other kinds of concentration of markets that reduce individual independent business people to mere economic serfs, and I think that is an important value that we have all too much lost sight of in our preoccupation recently in antitrust with economic theory.

The other point that needs to be emphasized about antitrust is the long-run concern with dynamics of markets. It is not the short-run efficiency that we need to be concerned with; it is how we maintain that kind of dynamic that has made our economy so successful over so many years, and antitrust needs to be focused on that.

Dr. Koontz has made some very good points in his paper about the kinds of things that can be done not just regulatorily in character, but in terms of other forms of market facilitation to facilitate those kinds of market dynamics.

Two points, then, about competition analysis that are important. The first, efficiency does not require any specific market structure. Senator Harkin quoted a little bit of my argument on that point, and again, Dr. Koontz's suggestions about ways to facilitate smaller-level producers is another example of the way in which we can facilitate market dynamics without having to go to behemoth-type industry. I would say the same thing about vertical merger as not being necessary to achieve some of the desirable effects of better integration between producers and processors.

The other point, and it is more directly responsive to Mr. Nelson, is that the prediction of economic theory about oligopoly is that there are going to be higher prices to buyers, lower prices to sellers, not that there is going to be higher profit. And when my late colleague, Len Weiss, went out and looked at the data on oligopolies, and I have cited his work on page nine of my presentation, he found overwhelmingly when you compared competitive markets to oligopolistic markets, what you found, higher prices, and mostly he was looking at selling markets, higher prices, not higher profits, so

that there is no inconsistency between the problems that we are seeing and a low level of profitability at the end of the accounting process.

We have stressed some of the changes in the market today. I want to reemphasize that in 18-years, we went from a beef market with four firms having only 36-percent to a market in which we now have four firms with 81 percent. So a clear failure of antitrust enforcement back in the 1980s which has resulted in that kind of structural change.

We have talked about other aspects of that change in terms of other parts of agriculture, and I want to emphasize the supply side, whether it is seeds—68 mergers in the seed industry in the last 5-years, or agricultural equipment, other kinds of supply.

Consequences, price margins are moving up, exactly as we would predict. Professor Taylor's work that I cite on page eight shows the most meaningful measure here is the difference between what the farmer gets and what the beef packer sells the meat for at wholesale, and those margins have gone up both in beef and in pork.

Growth in strategic behavior, and I describe a variety of the strategic behaviors that are going on in the markets today because of those high levels of concentration.

So it seems to me that we really do need to initiate some different kinds of policy responses, and I have outlined in my presentation three of those. The first is to enhance the enforcement of antitrust law, especially in the merger area, and proceedings like this that delicately prod the Antitrust Division to be more active are extremely helpful. When they know people are looking at what they are doing, they are, in fact, more likely to be active.

If you had this hearing 17-months ago, they would not have had a thing to talk about in terms of their enforcement efforts. They need to keep being prodded. And part of that, I think, is the kind of suggestion of bringing the Department of Agriculture officially to the table with some authority of its own to intervene in mergers when there is not an effective response from the Justice Department.

I did a lot of bank merger work when I was back in the Government and it was a useful interactive process between the banking agencies and the antitrust enforcers. I do not share the concerns that Mr. Rill has raised about dual enforcement in these areas. I think it actually can be a very effective tool. It is the competitive market in some sense being brought to bear on these problems.

I would also suggest, although the Senate is not the place to do it, that it might be useful to go back and take a look at some of those mergers that were allowed through in the 1980s. There is no statute of limitations under the Clayton Act and, therefore, it is possible to reopen those cases. There are good reasons why the Justice Department itself probably should not do that, but I think State attorneys general or others might give serious consideration.

Lastly, with the change in the market, and we are not going to restore the kind of competitive structure that would be optimal any time soon, it is important to bring, and it hurts me as a longtime antitruster to say this, but it is important now to bring more formal regulation to these business arrangements, and that is where, again, the proposals that are before you to expand the authority of

the Secretary of Agriculture to develop market facilitating regulation that will provide full information to buyers and sellers, that will facilitate the better functioning of the market, that are going to exist that are going to be increasingly contractual, is, I think, a very, very important step to be taken in this process. I would urge that there be a delegation, again, to an administrative agency. With all respect, I do not think the floor of the Senate or of the House is an appropriate place to write detailed regulation about how to contract for beef or pork or whatever.

I would, I guess, mention to you a very interesting experience I had a few years ago in Wisconsin serving on a committee of farmers and processors in the vegetable industry to develop the rules under which the contracting process would go forward. I think the end result of that were rules that structured that contractual arrangement in ways that were acceptable. I will not say everybody got what they wanted, but they were acceptable to both parties, and again, an administrative process is the way to get the actual participants together to develop workable regulation of the contracting structure.

One other point on the supply side, and it is a point I have been hitting away at. As we get more concentration in the supply side markets, especially the biotech ones, I urge you to take real care in looking at the kinds of uses that are being made of intellectual property rights in agriculture. Some of those strike me as being highly anti-competitive, highly undesirable, even if authorized by existing law. I have a student who comes from a farm in Iowa who brings me these contracts for soybeans and I look at them and I am wondering whether this is not an antitrust exam question that has escaped.

Let me conclude. We need robust competitive markets. They have been and must remain the centerpiece of our economy. Failure to preserve and protect them will result in serious economic and social cost. This is true in general and it is true with special emphasis in agriculture.

[The prepared statement of Mr. Carstensen can be found in the appendix on page 120.]

The CHAIRMAN. Thank you very much, as always, Mr. Carstensen.

Dr. Koontz.

STATEMENT OF STEPHEN R. KOONTZ, DEPARTMENT OF AGRICULTURE AND RESOURCE ECONOMICS, COLORADO STATE UNIVERSITY, FORT COLLINS, COLORADO

Dr. KOONTZ. Thank you, Sir. It is a pleasure to be asked to offer testimony on concentration in competition and the changing structure of agriculture, also to participate in this panel. Concentration and competition are an area that I focused most of my thoughts and research program on, and I have done this because I believe it is probably the most important economic and public policy issue that faces U.S. agriculture.

However, it has also been quite interesting to me to look at the interest with which producer groups and government associations, government bodies place on this issue over time. The public interest in this topic certainly waxes and wanes with profitability of

various sectors. It is my perception, though, that the underlying economic forces at work are pretty much—they pretty much remain constant over time.

The process of industrialization has ebbed and flowed with scientific and technological advancement, but the course has been quite steady. It basically started in pretty much the 1840s with international trade and has been on a slow, steady pace since then.

My view of how the different groups look at antitrust questions and concentration questions really highlights the need for an impartial observation where you back up a little bit. It is not my intent, certainly not my intent to make light of income problems that the farm sector is facing. We have had some pretty serious problems since the peaks of 1996 and thereabouts. Furthermore, these declines have been very widespread through a large number of commodities. The bottom line, though, is that these appear to be supply and demand related and not much related to industry structure.

So concentration, I do not see as the cause of the low prices and profitabilities, but I think there are certainly some issues that have cropped up that deserve some serious attention, in particular, market access by independent producers, market entry of firms with innovative ideas and addressing some of the policy possible inconsistencies that have contributed to this process over time.

So what are the economics at play and what does the published research have to say? It has been talked about here so far. You have basically two things to consider in a tradeoff. You have large firms that have demonstrated that they operate at low costs. However, the tradeoff in that case is those folks may have the ability to exercise market power and then that having a detrimental impact both on consumers and then downstream into the agriculture production sector.

That same question can be asked of the production sector itself, however. I think this is one of the key things that you get out of the 1997 census of agriculture. The graphs that we were shown with concentration in various processing sectors can be drawn for almost every production sector itself, including livestock, poultry, vegetables, grain crops. For example, if you draw that graph for fed cattle marketing, you get almost the exact same thing.

The research community has recognized this tradeoff and has spent a considerable amount of time trying to address it. There are a large number of research programs, academic programs, different groups that are devoted to discovery and communication on this topic. My take on it, what does the bottom line say? Basically, the cost efficiencies are orders of magnitude larger than the pricing problems that come along with the exercise of market power.

A lot of hay is made out of the increasing marketing bill, that gap between retail prices and farm-level prices. My take on that is that widening gap is almost entirely due to the cost of marketing services. Consumers are looking for more service, more quality and variety, more convenience. All of the declines in the farmers' share of the consumers' dollar are largely due to them producing a product that is pretty far from what the consumer is ultimately interested in.

Profitability, if you take a look at some of the base numbers on profitability in the agricultural processing sector, they are roughly 4, 4 ½-percent of net margins. That is the consumer dollar less the prices that are paid for the farm input. So we are talking about very low rates of return on these businesses. This was discussed earlier. Again, the proof in the pudding really comes out when you take a look at the stock market. These firms are definitely priced as slow growth, low-profit businesses.

Popular press has also made much hay out of high levels of concentration. Again, the bottom line there is that concentration translates into cost efficiencies, and that is largely what the research says is driving concentration. It is not the exercise of power. It is the capturing of cost and efficiencies, incorporating them and addressing them.

Some of the inconsistencies I have seen in economic policy perhaps are that we are targeting a lot of things towards dealing with economic viability of the family farm. As somebody who is probably going to be sitting on a tractor planting corn come Saturday, provided we get a little breeze blowing up through Virginia to dry out our sand hills, that is a real issue. But the legislation that is under consideration seems to be targeted at processors and market power, and from what I know of the research, there seems to be very little here to go after.

What about attempts to limit unfair trade practices? I think this is one of the precise problems with the P&S Act. It is just that defining unfair trade practice is a very expensive exercise.

I do not think the proposed legislation will have very much of an impact on margins, the marketing bill, or the farmers' share of the consumer dollar.

So what can we do? I just think antitrust legislation is not necessarily the right way to go with targeting this problem. One of the main things I see is providing some resources for price reporting, targeting improvements in price reporting. There is some support now for mandatory price reporting and getting the livestock and grain market news to do some of those things. That is not too consistent with what we were trying to do in the 1980s, which was get that function away from government services and into the private sector. The problem there is that price reporting, in my mind, is a public good and the private sector is not going to take it over very well, and I think that is coming home to roost some 10-years later.

Likewise, I think we need to do some serious looking at the market institutions that have to be in place that help markets work, and my prime example here are grading standards and the technologies that go along with that. I think a large part of contract production is simply due to the fact that quality control is impossible without it. You have to have quality control to make those things work. So the contract production is not so much to exercise power, it is to get the producer to grow a product that is more consistent with low-cost processing and more consistent with what the consumer is looking for.

Now, things are not all rosy at this level. I also see some problems in the beef industry in particular. Beef demand has declined since the early 1980s. It is a well-known fact. It is only recently that the beef packers have decided to do anything about this. Up

until this date, they have been trying to do the same thing they have usually done, only at a bigger scale and at lower cost. We have not had anybody that has come into this business and try to be innovative and provide some products that the consumers would find more acceptable.

So there is a problem that does come along with concentration, but I do think we can address some of these things by addressing the need to support public goods and the need to help with the public institutions that make trade work.

I think we are currently in the middle of a pretty big market failure, and that is indicative of increased concentration, more contracting, more vertical integration, but I do not think it is because of power. I think it is because of collective failure to protect innovation, to invest in these public goods, and to make the market institutions—to improve them such that they work so that you can have a competitive marketplace populated by independent producers. Thank you.

[The prepared statement of Dr. Koontz can be found in the appendix on page 139.]

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

Mr. Rill, your commission to examine these competitive situations with regard to international trade was commissioned, as I understand, by the Attorney General.

Mr. RILL. That is correct, Mr. Chairman.

The CHAIRMAN. And the Attorney General was apparently interested in our competitive situation with regard to other nations, vis-a-vis our export policies. Frequently in this committee, we talk about the salvation of American agriculture as the expansion of markets and the ability to knock down barriers, but at the same time to be competitive in terms of low cost and best quality.

I am curious as to what so-called anti-consolidation efforts that we have been discussing today here in agribusiness do with regard to the long-term export growth for farmers.

Mr. RILL. Mr. Chairman, two answers to that. First, the issue of market access was one of the three major areas of focus for the Committee. The report has been made available to the staff, and I do not think you want to go into the detail of that at this time.

With respect to the position of the United States in global marketplaces, our committee focused on antitrust enforcement. Our role was to advise the Department of Justice regarding antitrust enforcement in an increasing global economy.

One of the concerns that came up frequently, and we had a great deal of testimony on this, was that multiplicity of review of mergers and acquisitions, review overseas of U.S. transactions, review in the U.S. of overseas transactions, seemed to frustrate to a great extent mergers and acquisitions that might not have any anti-competitive consequence at the end of the day.

One of the issues that was raised as a matter of concern was the extent to which multiple agency review, review by sectoral agencies as well as by the antitrust agencies, inhibited mergers that would not necessarily have any antitrust consequence at all, could be approved by the antitrust agency and delayed on competition grounds by another sectoral agency, and that brought us to recommend that the antitrust agencies in the United States should have the author-

ity to review the competition consequences of a merger or acquisition. The majority would put it on a presumptive basis, or a preclusive basis. The rest would say, well, it should be at least presumptively binding on the sectoral agencies.

The interest in doing that was to clarify standards, reduce time, and not put friction in the system of the review of what would otherwise be considered to be pro-competitive mergers. The antitrust agencies, of course, would retain the full authority, as they have under current law, to prohibit anti-competitive mergers.

The CHAIRMAN. Mr. Carstensen has brought forward the general principle of antitrust that is important to consider in which he says, leaving aside efficiency for a moment, you do not want a king, you do not want a situation of tyranny or dominance in markets.

My question really goes more to Mr. Nelson and Dr. Koontz from just an observation in previous hearings that, unfortunately, agriculture does not have a very high rate of return on invested capital. As someone, as I point out anecdotally from time to time, who has 604-acres, I am worried about this because the rate of return on my farm has been perennially low for the last 40-years. This raises the question, why do you persist in this? There are other reasons other than the economic return. There have to be. There is not that much return even in a well-managed farm, but even then, we keep trying.

This is what Dr. Koontz is trying to point out, that even if you have something that has a very low rate of return, you keep trying to figure out new marketing strategies, mixture of things that you do on the farm, all sorts of new research that may lead to better seeds, better plants, or some breakthrough in procedure, because you have to do that in order to keep the thing alive unless you want to have a deficit situation.

But even after all of this, consulting with the Purdue people and having people combing the premise all the time, if you get to a four percent rate of return on invested capital, that, at least in my State, is pretty good. Even the very best of farmers would indicate that they tell the country banker or sometimes the regional banker 5 ½ and they impute capital gains over a 20-year period of time, three percent operational and maybe two-and-a-half percent capital gains. Now, clearly, that return is exceeded by Treasury bonds in almost any year without difficulties of international trade or anything else.

What we have heard from Mr. Nelson is that, unfortunately, this is not just a problem for producers, like me or Senator Grassley. It is a problem for everybody in the food chain. As a matter of fact, nobody is making money. This will come as a sad surprise to everybody who approaches the hearing looking for something else, but as a matter of fact, the markets have pretty well evaluated this year after year. The charge that Mr. Nelson has did not start in this year, and perennially, we are well below the S&P, we are well below the rest of almost any industry in terms of attracting new capital into our situation.

One of you made the point that your best bet was to invest in farmland, and some have observed before this committee that one reason why that works is because of Federal Government subsidies that bring rents higher. Through Federal policy, we have managed

to keep one asset, namely farmland, at a point at which we have some increase. Thus, my friends who go to the banker with imputed capital gains which are not obtained by the operation of that farmland, whatever may be its value.

This is a serious problem and it leads to cycles in terms of our hearings. For example, when we began the first of the four hearings, this being the fourth, during this Congress, I note from the Wall Street Journal this morning that pork bellies were below 40 cents in July of 1999. That is just 10 months ago. Now, I make that point because yesterday they spurted past $1 a pound, and this is within a ten-month period, a rather dynamic change in pork bellies. They settled a bit less than $1, but they had not been close to that point since 1996, which is often cited as a very good year for most prices, pork bellies included.

To what extent is this a problem of simply low returns, lack of innovation, lack of marketing skill, lack of the changes that need to be competitive, or is it antitrust. That is consolidation, because some of you are testifying, for example, on the issue specifically that one of our Senators has raised that you ought not to let packers own livestock, but one of you has said, well, if you do not, the quality control situation may suffer or supply chain or various other problems they have, they lose even more money if they do not have that control. Yet, this is very controversial up and down the road between farmers who have contracts and those who do not.

We have tried to attack the price transparency issue so there is a glimmering, as Dr. Koontz said, in terms of the public good. We got consensus, essentially, in a bipartisan way to do that. But we are still very deeply divided on this whole issue of contracting, on packers owning, on the idea that even failing businesses who consolidate because people sell out, losing farms sell to other farms. Now, this is concentration and it gets bigger all the time because people are losing money, and the failure to make money leads them to be vulnerable and to either sell or to abandon the whole process.

I was trying to raise with any of you philosophically what is our quest here? Is it a question of declining return and sort of no return really from that decline that seems to be persistent, or is it the consolidation situation, or how do you treat both in order to take Mr. Carstensen's point, no kings, no tyranny?

Mr. Carstensen, would you address this first of all since you have been quoted, and I hope accurately?

Mr. CARSTENSEN. Well, I think you have got hold of a very tough problem here because it is an interaction of market structures—and here I think is probably where I have got the biggest disagreement with others on this panel—structure does make a difference. Highly concentrated structures do create adverse consequences. I am not saying it is profitable for the dominant firm. In fact, if they do the same old, same old, because that is the way they think they can retain their position in the market, they may make matters even worse without enriching themselves. So that is where I think we need to be concerned with structure.

I am not saying to you that particular kinds of contracting should necessarily be illegal. What I want to point out is that contracting, as you get into concentrated markets, has a number of non-efficiency, non-quality objectives. They call them strategic ob-

jectives: exclusion of new entry, bettering your competitors, dominating your local region. Again, the end result may be that we all wind up as losers and that there are no winners.

So this is why, as I said, a little bit against my grain as a former Antitrust Division lawyer and longtime opponent of government regulation, I come here saying, we need better regulation to facilitate market relationships. And again, I think Dr. Koontz, who has focused much more of his attention on some of the details, has made some important suggestions that go beyond simply saying no, which is a little more where my mind was at, saying here is how you say yes. Here is how you facilitate useful contracting, useful new arrangements that will enhance the efficiency of agriculture.

At the end of the day, Senator, it may be that we have just got awfully good farmers who are very productive, a food processing system that is very efficient and carries it all through to the consumer at a good price, and there is going to be complaining because you are not making as much money as certain individuals, who I will not name, who happen to own monopolies. I think maybe the goal ought to be to look a little bit more at why some other industries are making high profits, is that really because they are so much more efficient or whatever, or is it because of market failure in other markets? That may be a more useful place to focus some of that attention.

The CHAIRMAN. Dr. Koontz, do you have any comment on this subject?

Mr. KOONTZ. Certainly. With respect to the legislation in particular, I really think that in reading it, not completely but trying to get the gist of it, it seems to me to be focused on prohibiting market power and motivated by that large margin between the consumer and the farm level, and I see that as a bit misguided, especially when you go in and look at the details. If you look at the details of returns to food processors, to the retail side, to the whole sector, you do not find a devil somewhere that is creating a problem.

This is the same problem you get when you start looking at structural linkages, levels of concentration and trying to link that to market performance. You get into trouble. Those links are pretty weak. What you really need to do is look at conduct, look at business behavior. I think this is why folks get so frustrated with the Department of Justice, that is what they try to do. They are in there looking at the details. What are people actually doing? The structure performance linkages just do not stand up in court because they do not identify who is doing what.

And to back up a little bit from a big picture, the corporate bashing that is going on, the big business bashing that is going on, I still believe that producers have a good bit of freedom to do what they want to do. As somebody who comes from a farm background, I know that is the case. As somebody who has an appointment in cooperative extension, works with producers extensively, I know that is the case. If you want to grow corn, beans, or cattle, you can do that. If you want to grow elk, buffalo, ostriches, emu, you can do that. You may have trouble finding somebody that is going to buy it, though, and I think that is what we have dealt with.

I mean, that is the real issue, is not that you do not have the freedom to do what you want to do. It is difficult to get it into a marketplace, and it may be difficult to get it in for good reason. For example, the contract limitations on the hog side are used as a lot of example. Those things are very well justified in some cases when you look at the inconsistencies in animals that can show up if you do not have some sort of arrangement outside of the marketplace, if you do not have some sort of contracting arrangement. And this gets into the grading system better and make the price reporting system better.

The CHAIRMAN. Yes, Mr. Rill?

Mr. RILL. If I may, Mr. Chairman, just very briefly, the focus of the legislation is in large part on mergers and acquisitions and to give another agency authority over challenging mergers and acquisitions. I do not think there is a case to be made that mergers and acquisitions have been permitted to go through that are anti-competitive in this sector. Structure is not to be ignored. I think the testimony of Mr. Carstensen that structure is being ignored is contrary to the guidelines set out in the merger review principles followed by the Department of Justice and the Federal Trade Commission. The fact is that structure is a starting point and only a starting point of analysis.

First of all, one has to define a market. Just take, for example, the metaphor that was used earlier, the four firms, let us say, assuming the accuracy, 80-percent in meat packing. First of all, is meat packing a market? It is affected by other markets, of course, so question whether that is a pure market. Even if it were a pure market, I just did some number calculation while I was listening to that testimony and I find that meat packing falls below the highly-concentrated level based on the numbers that were being used by some of your colleagues.

Under the Department of Justice and Federal Trade Commission merger guidelines, even assuming that markets were vacuum packed and not affected by other markets, then once one gets past structure under the guidelines, one has to look at other market conditions that permit the measure of vitality of that market such as competitive forces that are in play in the market, not only in the static but also in a dynamic way.

I think, over time, those guidelines have become accepted in the courts and understood by people that have to live with them and have to comply with them. To superimpose another set of standards in the merger area, it seems to me, is unjustified by the record and could be very injurious to the growth and productivity in this particular industry. But to suggest that structure is ignored or that dynamic analysis of competition is ignored ignores the dynamics of antitrust enforcement today and, I would say, in the 1980s. Thank you.

The CHAIRMAN. Mr. Nelson, do you have———

Mr. NELSON. If I may respond?

The CHAIRMAN. Yes, please.

Mr. NELSON. We are seeing integration across all industries because companies and industries are trying to take costs out of the supply chain. It is certainly not unique to the food industry. But

companies are linking together much more closely and some of that is being made possible because of information agriculture.

When Dell Computer gets an order for a computer, there is immediately an electronic impulse for the parts for that computer to all its suppliers. Dell actually never owns any inventory, but teleset up a system which you either buy into as a supplier or you do not.

Now, this is not irrelevant to the food industry. Wal-Mart has a system. You as a food company can play that game or not. A little more than a year ago, you would never see any Kellogg's cereal in Wal-Mart because they could not get their systems working with Wal-Mart's system. Wal-Mart is going to sell a lot of cereal whether Kellogg's is there or not. Kellogg's made sure they found a way to do that. That is what these companies are doing and information agriculture is making a lot of that progress possible. So much of this is an effort to take costs out of the supply chain which is inefficient. Thank you.

The CHAIRMAN. That is a remarkable analogy, that an order to a computer company that has no inventory triggers orders to all the suppliers simultaneously. Obviously, this is a good bit further than we are along in agriculture or in the food business, but as you are pointing out, Wal-Mart really dictated this with regard to cereal. Apparently to make the sale, you finally integrate with the system.

Mr. NELSON. All food retailers are trying to improve what they call their working capital efficiency. They are trying to sell a product before they have to pay for it, maybe several times. Pepsico likes to brag that a retailer can sell their Pepsi or their Frito corn chips several times before they have to pay for it, and that is a good deal for the retailer. So retailers are focused on this and you are buying into that system or you are not.

The CHAIRMAN. Gentlemen, we thank you very, very much for the outstanding papers that you have produced, all of which will be a part of the record as well as your testimony. Thank you for coming.

The Chair would like to recognize now a panel composed of Mr. John Greig, National Cattlemen's Beef Association of Estherville, Iowa; Mr. Jon Caspers, National Pork Producers Council of Swaledale, Iowa; Mr. Leland Swenson, President of the National Farmers Union, Aurora, Colorado; and Mr. Ron Warfield, President of the Illinois Farm Bureau, representing the American Farm Bureau Federation, from Gibson City, Illinois.

Gentlemen, having gotten you seated finally, it is my duty to say that a roll call vote just commenced on the floor. I, obviously, being the only Senator present, will ask your indulgence if I may to go vote, and that will take probably about 10-minutes in round trip. But having achieved that, then we will be back and look forward to your testimony in full. I apologize for this intrusion, but we will proceed as rapidly as we can.

[Recess.]

Mr. Greig, would you proceed with your testimony?

STATEMENT OF JOHN GREIG, NATIONAL CATTLEMEN'S BEEF ASSOCIATION, ESTHERVILLE, IOWA

Mr. GREIG. Thank you, Senator Lugar, for holding this hearing to discuss pending legislation on agricultural concentration and related issues concerned to cattle producers. I am John Greig, President of Greig and Company, a diversified family farming and cattle feeding operation in Estherville, Iowa. I am the past president of the Iowa Cattlemen's Association, and I should say that is very past president, and a member of the National Cattlemen's Beef Association [NCBA].

As with your oversight hearing in February, today's hearing offers another chance to closely examine the marketing structure changes occurring in the livestock industry and the concerns of the livestock producers seeking to maximize their returns in a very competitive marketplace. A growing number of cattle producers are finding innovative ways to compete in the changing beef industry while gaining a greater share of the marketing dollar. There are several examples of how this is going on and I would give you a few.

U.S. Premium Beef Limited in Kansas, Western Beef Alliance, the Iowa Cattlemen's Excel joint venture is a very exciting thing we will talk about a little bit, the Angus Alliance, Harris Ranch, just to name a few. There are several more.

I am a participating member and on the steering committee of the Iowa Cattlemen's-Excel joint venture. Six-months ago, a joint venture feasibility study was initiated between the Iowa Cattlemen's Association, Excel, and the State of Iowa to construct a new state-of-the-art beef packing plant in Iowa. Under the agreement, the Iowa Cattlemen's Association will be responsible for securing commitments from cattle producers for about 300,000 head of committed cattle required for this facility. These producers, who will be members of the Iowa Quality Beef Supply Network, and we currently have approximately 925-members from 98 of Iowa's 99 counties and from 12 other States, representing more than 330,000-head-of-cattle committed to this project.

Excel's responsibility includes estimation of staffing needs, engineering specifications, water supply, wastewater management, project development costs, as well as cattle purchasing and beef marketing strategies, and, of course, they will be the operating managers of the plant.

The State of Iowa, through the Iowa Economic Development people, will work closely with us, providing labor availability assessments, coordinated community involvement in working with other State and local government entities in site selection and other related issues.

The $100 million plant will focus on processing high quality, high-yielding cattle that perform well under the beef quality assurance and the beef safety concerns programs. The plant will utilize the latest in cattle carcass tracking and other technologies to provide valuable feedback to our producers. The plant will have 1,100 employees in a single shift, with a potential to expand to a double shift. Approximately 600,000 animals will be processed annually, and with a potential to increase that number as the plant size increases.

The Iowa Quality Beef Supply Network is the producer investment arm of the facility, created to secure annual commitments of approximately 50-percent of the plant's capacity for 5-years. In order to become a member, the producers had to pay a registration fee of $500, pay a $2 delivery fee up front, and commit themselves to between $50 and $100 a head for further capital investment as we begin to build the plant. Membership opportunities are still open and the network is accepting increases in cattle commitments from our current members, and I would say that what I personally thought might take 6-months to do, we accomplished in about 6-weeks. It was unbelievable, the interest we had in the project.

Some members are already benefitting from this participation through an interim grid available for those cattle that are tagged through the Iowa Quality Beef Program, and this grid works through the Excel Schuyler, Nebraska, plant, and during the month of February, 1,500 cattle were started in that process and we yielded about $24 a head more income off of that particular project. Again, we are picking up more and more cattle in that area as we go along and the producers seem to be very happy with it.

In all of these ventures, the participants are professional cattlemen and women who have come together in a proactive way to address their desire for growing a viable beef industry through bold new marketing strategies that enable them to capture a larger share of the retail beef dollar. Our efforts are focused on producing a better beef product marketed through our own beef companies and under our direction. We found that by working with one of the major packers, we thought we had a partner that could give us the expertise we needed in those areas of marketing, etc.

As part owners, we not only benefit from the rewards of the value-based pricing system, we also will be receiving earnings from the company. In addition, the data received by cattle producers from these efforts will assist our effort to continuously improve the quality of our livestock, which in turn can lead to additional market returns, and I think also very important, a better, safer project for consumers.

In conclusion, I think we all recognize the concerns that have led to the development of proposals regarding industry structure and competition. NCBA remains concerned about unintended consequences and urges a thorough analysis of the potential impact of these proposals. For example, the joint ventures mentioned earlier under a number of different business structures, and during my tenure as a State legislator and vice chairman of the Iowa Ways and Means Committee, I was particularly concerned about the tax implication that changes in laws and regulations can bring.

Let me give you a case in point using the ICA Excel joint venture. The firm of McGladrey, etc., in Des Moines, Iowa, one of our major accounting firms, did an accounting analysis of our project with Excel and we found that an LLC structure would provide a 14-percent return on our investment, where using an Iowa closed co-op structure, our return would only be 13-percent. The higher LLC return will be further amplified for producers because all of the income from a closed co-op is subject to self-employment tax, and under an LLC, only the income from cattle sales is subject to

that tax. So we must look carefully at how those issues interact with our business facilities.

NCBA and the beef industry support the Justice Department and the USDA enforcement of the Packers and Stockyards Act, as amended, and other antitrust laws and regulations. We urge that USDA be involved in premerger evaluation of proposed packer mergers in coordination with the evaluation by the Justice Department. NCBA supports a free market system and we trust in the ability and adaptability and innovating skills of U.S. cattlemen to prosper us in a relatively unregulated marketplace.

We do rely on Federal regulators to keep the playing field level by ensuring the marketplace is free from antitrust, collusion, price fixing, and other illegal activities that damage the viability of the market and interfere with market signals. If allowed to work, the market will recover with a minimum of government intervention.

We think that cattlemen, through very good innovative new joint ventures and other networking facilities, that what we need to do is to work in those areas and make sure that we do not confuse the issue by adding too many more regulations. Thank you.

[The prepared statement of Mr. Greig can be found in the appendix on page 144.]

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

Mr. Caspers.

STATEMENT OF JON CASPERS, NATIONAL PORK PRODUCERS COUNCIL, SWALEDALE, IOWA

Mr. CASPERS. Thank you, Mr. Chairman. I am a pork producer from Swaledale, Iowa, and serve on the Board of Directors of the National Pork Producers Council. Today, I am representing America's pork producers as we discuss the critical issue of agriculture concentration and its impact on pork producers and consumers.

Global competition, new technologies, and consumer demands are but a few of the factors that are rapidly changing the U.S. pork industry. However, while the pork industry is becoming more concentrated at every level, we continue to be less concentrated in the poultry industry or other livestock sectors. Concentration in the pork packing sector has grown from 32.2-percent in 1985 to over 56-percent in 1998, while concentration in the production segment has grown from negligible levels in the early 1980s to about 18-percent today. Vertical integration, or the percentage of hogs owned by packers has gone from an estimated 6.4-percent in 1994 to roughly 24-percent today.

NPPC has launched a number of new initiatives to help ensure that producers have a fair, transparent, and competitive market. We firmly believe that access to information and knowledge will form the foundation for guaranteeing long-term market competition. That is why the National Pork Producers Council [NPPC] has focused so much effort in the areas of information dissemination and in helping producers understand and make use of that information to make knowledge-based business decisions.

A large number of these initiatives were designed and implemented by NPPC's price discovery task force, which I currently chair. These initiatives include development of a packer price reporting system that focuses on actual procurement costs, also a

passage of the Mandatory Price Reporting Act of 1999, the NPPC producer price reporting initiative, which encourages producers to negotiate with more than one packer and to report the price to USDA. Our recent publication of our guide to marketing contracts, whose goal is to help producers make more informed decisions about marketing contracts and their terms, and also NPPC has conducted with the University of Missouri live hog marketing studies in both 1999 and 2000. And all of these actions potentially have increased the information for and the knowledge of producers.

In addition, NPPC facilitated the creation of a national producer co-op called Pork America. Pork America's goal is to find new marketing and other value added opportunities for producers.

Concerns over the possible market distorting effects of concentration led to a number of resolutions being considered and passed during the recent 2000 National Pork Industry Forum. Delegates supported a study of the structure and competitiveness of the present hog market by USDA. They also supported a review of the definition of price discrimination and the Secretary of Agriculture's authority to challenge price discrimination. They supported a USDA study of justifiable price differentials, a study of the Department of Justice concentration threshold levels to determine whether they should be revised.

They also supported continued scrutiny of the packing and processing industry to assure adherence to relevant Federal antitrust laws and the passage of new laws, if necessary, new authority for USDA to review and make recommendations to the Department of Justice regarding approval or disapproval of agricultural mergers, acquisitions, and consolidation of agricultural input suppliers. They supported the USDA authority to require agribusinesses with more than $100 million in sales annually to file information related to corporate structure, strategic alliances, joint ventures, etc. Also, the establishment of a Deputy Attorney General for Agriculture, which has been accomplished. And also, they support new legislation that requires processors to bargain with producer cooperatives.

In summary, Mr. Chairman, concentration is a complex issue. We hope that the Committee will approach it in a cooperative manner, similar to issues like the mandatory price reporting and interstate shipment of State-inspected meat.

I must express our concern, however, that neither Congress nor the administration has yet to provide the remaining $1.35 million for the Mandatory Livestock Price Reporting Act to ensure that USDA can carry out its full legislative mandate in a timely manner, and this must be done soon.

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

That concludes my comments, and thank you for the opportunity to share the pork producers' views on this issue.

[The prepared statement of Mr. Caspers can be found in the appendix on page 152.]

The CHAIRMAN. Thank you very much, Mr. Caspers. Let me just interject parenthetically, the Chair and the Committee share your frustration over the inability of USDA to move on to our information legislation. There are good reasons for that often expressed, because we raise the question with the Secretary and with others whenever they come, but we will be persistent and we appreciate your raising the issue again.

Mr. Swenson.

STATEMENT OF LELAND SWENSON, PRESIDENT, NATIONAL FARMERS UNION, AURORA, COLORADO

Mr. SWENSON. Thank you, Mr. Chairman. I appreciate the opportunity to appear before you and the Committee to address this very important issue.

As I travel the country, outside of price, concentration probably rates second to the issue of concern to farmers and ranchers throughout the country. It rates higher than the concern right now of rules and regulations, trade, or bigger than taxes. I just want to emphasize that because that is where farmers and ranchers are putting the issue of concentration.

I want to say that I believe we can address this issue, and I will say that I think your leadership and efforts you showed last year in bringing together a bipartisan effort on mandatory price reporting can be an example that you can use, Mr. Chairman, in leadership in addressing the issue of concentration.

A year ago, the National Farmers Union commissioned the Heffernan report on concentration and I would like to enter it as part of the record so that it can be there to be the example of what is unfolding.

The CHAIRMAN. It will be placed in the record in full.

Mr. SWENSON. I think you shared with the previous panel examples of what has unfolded in the structure of agriculture from that of the changes that have occurred in production agriculture to the changes that are occurring from input supplies for producers to that of market opportunity. The industry is becoming very concentrated. A number of things unfold in this. We see the control from gene to fork and the impact that it has on farmers. It is not only domestically, but it is internationally.

You said, Mr. Chairman, that we are dependent on exports, and when we take a look at history, about 30-percent of our production needs to go to the export market. But what we have seen happen over the last 30-years is that percentage has stayed stagnant. We have not had a growth over the last 30-years, since back in 1975–79 annual average. But what we have seen happen is that on the competitive commodities which we produce here, a significant increase in imports, so that the real reality of what our export percentage is down to about 10-percent. What we see happen on the nature of concentration is that we see more firm-to-firm trading occur rather than a true competitive export situation that is in place and the competition under the structure of trade agreements.

I want to highlight a couple of things in relation to some previous testimony. First of all, for the record, is a copy of a letter written by myself on September 7, 1999, and again on October 14, 1999, to Joel Klein at the Department of Justice expressing our op-

position to the Smithfield/Murphy merger. If there was any consultation with farm groups, we had a clear written position in opposition to that proposed acquisition.

Mr. SWENSON. The second thing I would point out is that does DOJ review in its divestiture process the fact that if a local elevator is sold, does that sale, if it is sold to a private individual or to a co-op or to any entity, does it include a marketing agreement which requires that cooperative to market all the product they procure back to the seller, in other words, back to a Continental or a Cargill or Bunge or whoever it may be, because then we have not created, even through divestiture, real competition for the marketing of agricultural products for the farmers in that community.

The other thing I want to point out in the area of what we see unfolding in the structure of even production agriculture under contract is that farmers find little capital on the margin of return which you mentioned you get on your farm and I have on my farm. There is very little margin. And so we find ourselves in a dead obligation to contract for the production of grains or livestock, and what we have happen is that there is very little risk in speaking out against ramifications of that contract, number one, afraid of losing that contract and not having anywhere else to either procure the commodities with which to produce and/or market the commodities if you can produce it.

So as we take a look at what can be done, I urge, Mr. Chairman, your leadership in combining the Grassley bill with the Daschle–Leahy bill to bring forward a bill to pass out that begins to address whistleblower, compensation, USDA oversight with enforcement opportunities.

I also urge you, Mr. Chairman, to pass Senator Johnson's bill to ban packer ownership of livestock. If we truly want to have a free market, it has to be a competitive market. It has to be a competitive market, and the right for producers to own the livestock to market into the processing sector.

Third, we need to pass the interstate shipment of State-inspected meat and the poultry bill that has been introduced by Senator Hatch and Senator Daschle. You set the example last year in bringing forward a bipartisan effort on mandatory price reporting. It was appreciated by those of us in production agriculture. We look for your leadership in addressing the issue of concentration. Thank you, Mr. Chairman.

[The prepared statement of Mr. Swenson can be found in the appendix on page 158.]

The CHAIRMAN. Thank you, Mr. Swenson. You are very generous in your recollections of our work. Nevertheless, I appreciate the point you are making.

Mr. Warfield.

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

Mr. WARFIELD. Thank you, Mr. Chairman. My name is Ron Warfield. I am the President of Illinois Farm Bureau, a member of the Executive Committee of the American Farm Bureau Federation. I have a farming operation in Gibson City, Illinois. I am a corn and

soybean farmer, but used to be a cattle feeder like John Greig in my previous life, I guess.

I am testifying on behalf of the American Farm Bureau Federation today, and as you know, we work very hard to grow the marketplace and we have two very, very important issues that are coming to bear immediately ahead of us, what we are going to do with PNTR to expand the marketplace and what we are going to do with ethanol to expand the marketplace. We are very much for expanding the markets, growing the markets and saying that is where our increase has to come from.

At the same time, producers must have confidence that once we have those expanded markets, that markets still work. And the question that many of our producers are asking today is, is price discovery there? Is there competition? And is the marketplace working, not just at low prices, but also at high prices?

Farm Bureau believes that consolidation and subsequent concentration with the agricultural sector is having adverse economic impact on U.S. farmers. We believe Congress must review existing statutes, develop legislation where necessary, and strengthen enforcement activities.

Since last fall, we have worked to develop legislation which would reduce the adverse impact of concentration on agriculture. We have worked very closely with staff members from Senator Leahy, Senator Daschle, and Senator Grassley's offices, and we sincerely appreciate your leadership and interest in holding these hearings and this issue and we are extremely grateful for the untiring efforts of the Senators in crafting legislation to address our concerns. Today, Farm Bureau asks members of the Committee to continue to make this issue a priority and to reach a bipartisan solution to address concentration in agriculture this year.

Many of the concepts proposed by Farm Bureau have been included in either the Daschle–Leahy bill or the Grassley bill. Our priorities are for legislation to move this year and for increased involvement in the consolidation issue by the USDA. Farm Bureau would like to see an expanded role for USDA in evaluating agribusiness mergers and acquisitions, which currently are under the jurisdiction of the Department of Justice. We believe broadened USDA responsibility and official consultation with DOJ will ease much of the concern regarding the concentration of agribusiness.

And I must say, in the last year, we have had numerous groups to visit with both the Department of Justice and the USDA. I have done it personally and I have had our board members out here to do it, and our concern is, even though it is expressed that there is that interaction, we found in direct meetings, one following another, an official from USDA would point the figure and say, oh, that is over in the Department of Justice, and then we talk to the Department of Justice and they said, oh, that is over in USDA, and the finger pointing went on all day. We believe we need legislation because it is not happening administratively.

USDA is uniquely positioned and qualified to offer a thorough economic analysis of any proposed merger or acquisition, and this analysis should be made available to the public and other government agencies. We are very interested in the model currently being

used by the Surface Transportation Board and we will look at that model as one that we could use in saying how we would interact.

We would like to see the following additional actions considered in the concentration debate. The Grain Inspection, Packers, and Stockyards Administration may need additional resources to investigate anti-competitive pricing. Farm Bureau members would like to see better publicizing of these investigations, the results of the findings, and whether civil penalties were imposed. And when we were here visiting with them, they indicated they had two litigators, two junior litigators, on staff and certainly were not able to handle the load that they had.

GIPSA should be able to evaluate actions taken by packers who purchase plants and then shut them down. In the last month, we have heard from our Northwestern Illinois hog producers when Smithfield announced that it should shut down the hog processing line once it purchased Farmland's Dubuque, Iowa, pork plant—a good example. This action may result in substantially lower prices for producers of the 7,800 hogs that are processed or slaughtered each day at that plant. Recall at your February hearing that a Purdue agricultural economist indicated any further reduction in the numbers of packers could certainly have a negative impact on hog prices and the competitive nature of our marketplace.

GIPSA should be allowed to ask for reparations for producers who can show damage as well as civil penalties when a packer is found to be engaged in predatory or unfair practices. Contract poultry growers should be provided the same protections as livestock producers by extending the powers of Grain Inspection, Packers & Stockyards Administration [GIPSA] to cover live poultry dealers in the same fashions as packers of cattle and swine are covered. Farm Bureau has long supported authorization for a statutory trust for the protection of cash sellers to livestock dealers.

We need more transparency. Farmers need more information about mergers, acquisitions, and anti-competitive activities, and of prices, and of prices at all levels.

Farm Bureau supports appointing an Assistant Attorney General at the Department of Justice with the sole responsibility of handling agricultural mergers and acquisitions. We support an increase in the staff of the Transportation, Energy, and Agriculture Section of the Department of Justice. The enforcement of confidentiality clauses in livestock and grain production contracts should be prohibited except to the extent that a legitimate trade secret is being protected.

USDA should be required to assimilate, maintain, and disseminate upon request detailed information relative to corporate structure, strategic alliances, and joint ventures for all agribusiness entities with annual sales in excess of $100 million.

And lastly, producers may need government assistance to develop co-ops that will add value to their product and legal structures that will help them develop relationships with other producers to pool resources to compete in today's economy. We started privately a producers' alliance in Illinois to facilitate producers performing such activities, like John Greig mentioned on the beef initiative, or what was mentioned in terms of happening in pork.

Thank you for the opportunity to provide this information on this important issue, and let me say again, we appreciate your efforts to address these issues and look forward to working with you in the future to obtain a bipartisan solution.

[The prepared statement of Mr. Warfield can be found in the appendix on page 164.]

The CHAIRMAN. Thank you very much, Mr. Warfield. It is good to have you, as always.

Let me just say that when we had this hearing or a similar one a while back, we had testimony from Professor Parlberg at Purdue, who was suggesting that there had been more concentration in the pork industry—I think that was the model he was centering on that day—and that one of the ways in which producers might gain more bargaining power and change price would be through very large co-ops. He also suggested, if I remember correctly, as many as 300,000 head of hogs would be required to command maybe one or 2-days in the marketplace sufficient to make that kind of a change.

That has not come to pass in my home State of Indiana, but nevertheless, his model is not unique and each of you in a way are reflecting the fact that, pragmatically, producers in Iowa, for example, both in cattle and hogs, are trying to think of how you can get greater marketing power in different ways. You suggested, Mr. Greig, through working with this company in which you are now part owners and, therefore, having a share of the flow of revenue, hopefully profits, that come from that situation in addition to what, as I heard you, about $24 a head better in terms of your pricing. But this is a very complex arrangement as you have described it, not easily come by and not altogether readily accepted by everybody who is a cattle producer or a hog producer. There are many farmers, and you have to respect this point of view, who say, we do not want to be a part of a large cooperative, or we just really want to have an independent view of the market and handle our situation as we always have.

How all that will be compatible with life in the times, I do not know. This is what we are trying to sort out, because many producers are making arrangements in cooperatives or in combines or cooperation of some sort, however it is described.

Mr. Warfield has given a set of principles from the Farm Bureau, many of which, I think, are shared by most members of the Committee in a bipartisan way that would filter through legislation to get regulations if we are unable to get legislation, or influence the departments.

Can any of you give sort of an overall perspective of where we are headed in the markets with respect to not consolidation of producers but cooperation of producers as a counter to perceived consolidation of packers or agribusiness firms, because Professor Parlberg, and he may be incorrect, said probably we will not turn the clock back. A suggestion was made by Dr. Carstensen that conceivably there is no statute of limitation on these things. The Department of Justice could take a look at something that occurred in the 1980s or early 1990s or what have you, when the allegation is that perhaps antitrust enforcement was less vigorous, and that might occur.

But then there are unintended consequences and dislocations. Mr. Greig has said from his own experience as a legislator trying to take a look at these things, you have to walk around it as to what kind of harm is done, what sort of damage occurs even while you are trying to get absolute justice.

So if we accept the fact that probably we have a fair degree of concentration, is this an appropriate way to go? Is this likely to occur with regard to cattle and hogs? The chicken and poultry people usually come in with different kinds of testimony on these issues. If they were here, I suspect there would be some variation from what we have heard. But do any of you want to forecast? Yes, Sir?

Mr. GREIG. Yes, I would like to make a comment that even though we are looking at a joint venture with a major packer, there are some side issues that help those that do not want to join us, and that is that, number one, only half of our facility will be used for our own cattle. The rest will be bid onto it in the open market. And as a result of that, we have brought a second packer into the major Iowa-Illinois market. So there is a competitive thing that has come up in this issue.

The case in point would be that IBP was our only market in my area and a lot of people east of me, and as soon as we started to bring this together, those bids changed and their attitudes changed. So competition was immediately thrown into it.

The second thing that I think is very important, half of that company will be owned by us. It is a 50–50 operation. There will be, of course, cattlemen members on that thing and we will have to answer to the Iowa Cattlemen's Association and the rest of the producers in the State and we feel that as we look at the board, that those board actions will be pretty well publicly known and I think that information will be free flowing, and that is one of the objectives we wanted, is the free flow of information, so that we hope that we can take some of those iffy issues out and they will become knowledge at least to the professional cattlemen in the State of Iowa and our surrounding States.

The CHAIRMAN. Mr. Caspers, you are representing obviously the national group today, but you are sort of side by side with your colleague out there in Iowa. Are things working along for the pork producers in a similar way, or how would you describe your situation?

Mr. CASPERS. Well, with the last 2-years, the economics we went through in the pork industry, there is a lot of interest amongst producers in that kind of activity, and as I mentioned in my testimony, the National Pork Producers facilitated the formation of Pork America, the pork co-op, if you will, that is currently going through a producer signup membership process, so I do not have a lot to report there at this time. It has taken a lot longer than they had hoped because of the registration requirements all across the country.

The CHAIRMAN. How readily is it being accepted? Are people going to sign up in this, or———

Mr. CASPERS. I can report, I guess, a little more currently on the local level. In Iowa, we also have a pork co-op effort of which I am a member, and recently, the Iowa Premium Pork Company com-

pleted their membership drive and signed up over 1,400 producers as of the end of March and representing several million pigs of production. So there is a lot of effort in there. Their intent initially will be to do some group marketing from the standpoint of having a larger volume and the ability, hopefully, to garner a better price, but in the long term to sign and make some agreements with the existing packers to provide particular products for particular markets.

The CHAIRMAN. Mr. Swenson?

Mr. SWENSON. Thank you, Mr. Chairman. I think the critical thing is that there is probably not one option or one idea that has to be looked at. I think it is going to take cooperatives, it is going to take lender liability corporations, it is going to take LLPs, it is going to take a whole different structure of which to truly create what I would like to call a competitive marketplace, where an opportunity for independent producers of which to market livestock or grains through.

I think the challenge facing many of the producers to create alternatives is access to capital and the cost of the capital. It is more available to Excels and Iowa Beef and those types of entities than it is in the cost of capital for individual farmers to go and try to form a new cooperative or a new limited liability corporation.

So one of the biggest hurdles to deal with is the cost of the capital and the access to the capital. The other is the access to the market for the finished product, because we are seeing in our analysis and our study of the retail market, the retail market is becoming as concentrated as the processing sector. And so there are now agreements that are being signed between Excel and Wal-Mart, for example, that they will agree only to accept certain products from certain companies for shelf space and then denies the access for new ventures that wish to have access to the public market. So that is an issue that also is associated with the investment that you create within that processing structure.

So one of the things I will commend the Department of Agriculture in establishing, and that is for low-equity producers out there. They will borrow money for stock investments in some of these new cooperative venture opportunities, and I think that is a positive step for producers to be able to help themselves.

The CHAIRMAN. Mr. Warfield, do you have a further comment on this?

Mr. WARFIELD. As I said in my testimony, I see a lot of interest among producers in terms of the value added and very interested in terms of participating in that. Certainly in the hog sector, they have lost a lot of equity in the last 2-years and so some of the enthusiasm for investing is there but the dollars are not.

The other point that I would like to make in that regard is that when Professor Parlberg testified, he said we also cannot allow further concentration in the packing industry on the hog side without deterioration in terms of competition for live hogs, and certainly as we look at that, we are going to have a time period in here for this competition to take place, and so I am very concerned about what would happen in the interim relative to further concentrations, and I mentioned the one with Smithfield.

The other point I would like to add, if I may, is the fact that, as you mentioned the poultry industry, and the one thing that happened when we had the poultry industry consolidating was we had price discovery taking place at the retail level and we knew what the nine city weighted retail price of broilers was. Today, try to get that same information for pork or beef and it is not available. And if price discovery is going to take place at the retail level, as we move more and more in that direction, if markets are to work, I think we need that kind of information available so that we can be producing for that marketplace.

The CHAIRMAN. That was a point made also by Dr. Koontz in our previous panel, this public good that this committee, the Congress, and hopefully the administration will try to help provide, which we are still striving to get from even the legislation that we passed last year that you have commended.

Let me just make a sort of a short report to this panel, but likewise to the press and other observers because the question will obviously arise after all of you have labored for 4-hours this morning on this issue and wonder what is going to happen.

Essentially, on Tuesday, the majority leader, Senator Lott, had a meeting of committee chairmen in which I participated representing this committee and indicated that, by and large, that the remainder of the session will be spent attempting to pass 13 appropriation bills so the Congress does not come to September 30 with some unpassed and some sort in sort of triangular negotiation with the White House during October and the preelection period. But this means an acceleration of activity with regard to both the Appropriations Committee and floor activity.

So the quest was, what is your must legislation, because there will be very few slots available and in most cases only for bills that are almost a lay-down hand in which you get unanimous consent or certainly no threat of filibuster or extended debate or difficulty.

Ahead of us right now as a priority, of course, is the conference on crop insurance risk management in which staff had been working throughout recesses that the Senators and members of the House have had. We are making good headway and I predict success, but we are not there and there are a lot of issues in risk management and crop insurance and some even being added as we speak. So that, really, we will need to get done, and we have to reserve some time to do that.

Likewise, we have this very serious issue of MTBE and ethanol that was a part of our hearing a week or so ago, how that is to work out both with regard to the environmental community and committees that are involved in energy and the environment and us is difficult to tell, but important. There are time frames here involved, not only with the California MTBE but with other States that have something beyond agriculture. But we have quite a stake in that with the ethanol quest, both from corn farmers or maybe ethanol from other sources. So whether that is a go or a no go, I do not know, but it is very important and we are trying to work on it.

We have this CFTC authorization, and the draft of that legislation will be apparent next week. Large issues of contract certainty with regard to certain markets, the Shad–Johnson accord, a num-

ber of decontrol aspects. I have worked now closely with the Chairman of the Banking Committee, Senator Gramm, who has great interest. This has been historically where things came to a stop in the past, the Banking Committee with its interest in the SEC and this committee with interest in the CFTC got crosswise and no one moved. So we have gone through several Congresses on occasion without reform and kicked the can on reauthorization without much change, but we cannot do that anymore because our markets are going to Europe. The effectiveness, at least, of the price discovery that we take for granted in agriculture, quite apart from other markets, may be happening elsewhere, as we saw displayed electronically at one of our hearings.

So we need to move on that, and that is a big bill. Attempting to get all the parties on board on that so we do not have a large floor fight will take some doing, but it is conceivable.

Now, in addition, we have had earlier the problem of agricultural sanctions. We passed a bill out of this committee that would exempt food and medicine. That is still out there on the floor. The leader thought he was going to give me an opportunity to deal with that even this week, but events in Cuba, essentially, have postponed that temporarily, so we shall see whether it can reemerge. But in one form or another, the sanctions issue is a very big one in terms of our exports as well as American trade generally.

We had 2-days that were promised to Senator Kohl, Senator Grams, Senator Wellstone, and others on dairy policy. Now, essentially, we have been busy with the Committee, trying to come to some consensus. It is not a supreme court in which we all offer our opinions, but it comes much like that with regard to dairy policy, in which the Chair is not aware of any majority on any policy, although some members are asserting that they are sure they have the votes if we actually had a meeting and everybody had to vote. But in any event, it is there and it is an important issue on which many members feel very, very strongly we ought to move forward.

The possibilities of passing a two-house dairy bill and a Presidential signature, I think, are not great, but that is not my judgment, and my style has not been to make these judgments and to say simply we will not discuss it. We will discuss it, but it is not apparent we have consensus.

That is true, likewise, with regard to sugar loans and other things that now are bedeviling the Secretary as he tries to decide what to do in that area, not necessarily a legislative proposal at this point, but nevertheless I visited with the Secretary now at some length about this. He has gone to China and is mulling it over while he is there, I suppose. He will come back and it will still be here and we will be thinking about that.

In addition to that, we have, obviously, the concentration bills that have been discussed today and the need to coordinate with the Judiciary Committee. We had some communication, as you noted, in the first panel, as members were exchanging papers and some heading off to Judiciary even as we were dealing with that here, and it is a serious issue there. We will have to visit with Senator Hatch, who is the Chairman. Senator Leahy, of course, our member, is the Ranking Member of the Committee. Senator Grassley is involved in that venue, as well as this one. Senator Daschle and

Senator Johnson have been active in this committee in addition to that.

I am just trying to sort of sort out for all of us where all that stands, and I do not know for the moment, but we will certainly be assiduous in attempting to move ahead on all of these as to that which is possible. At the end of the day, we will get some floor time, I hope. If we do not, some of this may appear as amendments on appropriations bills, which will be test votes for members but probably not legislation. This is why we have tried very hard to keep the integrity of these bills as we have them so they can be considered on their merits as opposed to test votes of finding out where people are. But the Senate is a free-wheeling situation. There are no germane situations ultimately with regard to amendments, so some of this may appear in that form if it does not come through the regular sources.

I thank you for indulging me in giving this summary because some of you might ask whether concentration or other things on which you have testified—many of you have been before this committee on several occasions this year offering testimony for your organizations. We thank you very much for your patience and your endurance, and the hearing is adjourned.

[Whereupon, at 1:09 p.m., the Committee was adjourned.]

APPENDIX

April 27, 2000

Chairman Richard G. Lugar

U.S. Senator for Indiana

Opening Statement on Agriculture Concentration

Today the Senate Agriculture Committee is holding a hearing on two matters. The first is the confirmation of Michael V. Dunn to be a member of the Farm Credit Administration Board. The second will address concentration and competition in agriculture

First we will turn to the confirmation of Mr. Dunn. A native of Iowa, Mr. Dunn currently serves as the Under Secretary for Marketing and Regulatory Programs at the U.S. Department of Agriculture. Prior to that he was the Deputy Under Secretary for Operations and Management in the Rural Economic and Community Development mission area at USDA. Additionally, Mr. Dunn served as Administrator of the former Farmers Home Administration at the Department of Agriculture. Mr. Dunn is no stranger to this Committee; from 1987- 1988, he worked as a professional staff member under the chairmanship of Senator Leahy.

The availability, efficiency and affordability of agricultural credit remains an important issue to the members of this committee. As a member of the Farm Credit Administration Board, Mr. Dunn will play an important role in the future of farm credit.

We are pleased to have him before the Committee today and look forward to hearing from him. Before recognizing Mr. Dunn for his statement, I would like to turn to Senator Harkin for any comments he would like to make.

Today, the Senate Agriculture Committee will conduct the fourth in a series of hearings in this Congress addressing concentration and competition in agriculture.

The Committee has previously heard testimony outlining the potential cost and benefits accompanying consolidation and coordination in agriculture. Witnesses have told us that the benefits include higher quality products available at lower consumer prices and more efficient use of production resources, enabling resources to move to production of other products, thus increasing the national living standard. On the cost side, witnesses have testified that consolidation has negative impacts on environmental quality, economic viability of small farm and firm operations, and rural communities dependent on agriculture.

The Committee has received testimony from Joel Klein, the Assistant Attorney General for Antitrust at the Department of Justice. Mr. Klein told the Committee that the Department of Justice possesses adequate authority to execute antitrust laws, the question is using them properly. However, recent consolidations continue to raise questions about concentration and antitrust enforcement.

Today's hearing will explore what tools are necessary to facilitate the enforcement of laws prohibiting unfair business practices and which federal agency is best suited to execute these laws. The Committee will also consider what role the U.S. Department of Agriculture should play in the agribusiness merger review process. Currently, reviews of mergers and acquisitions within the agribusiness sector occurs with the Federal Trade Commission and the Department of Justice. These agencies often call upon the USDA to provide expertise and data on pending reviews. There are proposals before the Committee which formalize USDA's role in the merger review process. Those proposals do other things such as establishing a commission to review claims of family farmers and ranchers who have suffered financial damages due to unfair business practices. Also, these proposals require large agribusinesses to report on their corporate structure describing domestic and foreign activities.

Mr. John Nannes, the Deputy Assistant Attorney General at the Department of Justice, will provide the Committee with a progress report on the newly created position of Special Counsel for Agriculture within the Department of Justice.

I welcome Mr. James Rill, formerly the Assistant Attorney General for Antitrust and, who more recently, was appointed by the Attorney General to chair the International Competition Policy Advisory Committee, whose final report was completed in February. I welcome Mr. David Nelson from Credit Suisse First Boston. Mr. Nelson will provide the Committee with an analysis of the performance of agribusiness on Wall Street.

Also presenting testimony are Dr. Steven Koontz from Colorado State University and Mr. Peter Carstensen from the University of Wisconsin. Both have done extensive research on the issues of agriculture concentration and antitrust law.

Today's third panel contains Mr. Ron Warfield from Gibson City, Illinois, representing the American Farm Bureau Federation, Mr. Leland Swenson from Aurora, Colorado, President of the National Farmers Union, Mr. John Greig from Estherville, Iowa, representing the National Cattlemen's Beef Association, and Mr. John Caspers from Swaledale, Iowa, representing the National Pork Producers Council.

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STATEMENT OF SENATOR CHUCK GRASSLEY
Senate Agriculture Committee
Hearing on AG Concentration
April 27, 2000

Thank you, Mr. Chairman. I want to express my appreciation to you for holding this hearing which focuses on AG Concentration. Specifically, this hearing will examine legislation that has been introduced to address AG Concentration such as my legislation, S. 2252, and legislation introduced by committee colleagues, Senator Daschle and Senator Leahy. I believe this hearing is the first step toward meaningful action on AG Concentration.

As well all know, attention on AG Concentration has become especially focused within the last 18 months to 2 years. Record low prices for many AG commodities and a wave of agribusiness mergers have led anyone who is deeply involved in agriculture to take a serious look at the infrastructure of agriculture and whether it is conducive to the survival of the small, independent producer.

Small farmers see their place in the food production chain becoming less and less secure. That's why, especially in the midwest, we have seen huge turnouts of farmers at meetings to discuss Ag Concentration and what it means for independent producers. Over a thousand showed up at a meeting in Minnesota last spring and we had 350-400 show up at a meeting I sponsored with my colleague, Senator Harkin, in Cedar Rapids late last summer. It is also striking to note that at these meetings, farmers came from a multi-state area; it wasn't unusual to find producers who had come hundreds of miles to express their concerns about concentration.

I've had farm bureau officials tell me that concentration is a topic that comes up at nearly every county meeting they have. It was this outpouring of concern that prompted me to take a look at what Congress could do regarding concentration and ultimately to introduce legislation earlier this spring. I believe my proposal is reasonable, workable and necessary.

I'd like to briefly summarize my bill. S. 2522 would require the Department of Agriculture to do a review of proposed agriculture mergers. USDA would have the mission of assessing whether a proposed merger would have a substantial detrimental effect on producers' access to the marketplace.

This review would be conducted simultaneously with the review done by the Department of Justice. Furthermore, my bill makes no changes to the anti-trust review

process or standard used by the Justice Department.

If USDA believes the merger would have a substantial detrimental effect on farmers' access to the marketplace, then USDA would be able to enter into discussions with the merging parties to address those concerns. If those discussions are not successful, my bill gives USDA a very narrow timeframe in which to decide whether or not to pursue a challenge to the merger, even if DOJ has approved the merger. If USDA goes forward with a challenge, USDA must make its case in Federal court. If USDA wins in the impartial forum of a Federal court, then the merger is stopped or conditions are imposed on the transaction.

My bill also calls for the appointment of a special counsel for competition matters at USDA and an Assistant Attorney General for Agriculture anti-trust matters at DOJ. The legislation also expands the authority of USDA's packers and stockyards division, to investigate anti-competitive, unfair or monopolistic practices in all commodities. Currently, packers and stockyards' authority pertains only to the livestock industry. Producers in all AG sectors have told me that additional authority for packers and stockyards is needed. Finally, among other items, my bill prohibits contract confidentiality clauses that prohibit AG producers from getting the advice they need to make the best decisions for themselves while at the same time protecting legitimate trade secrets. My legislation is based to a substantial degree on the AG concentration plan put together by the largest AG producer organization in the nation, Farm bureau.

My bill has been quite controversial. Some believe that my bill is anti-agribusiness. However, I've worked on a farm practically all my life; I made my living as a farmer for many years before I came to Congress.

No one knows better than I that a farmer cannot do his job without the agribusinesses that produce the seed, fertilizer, pesticides and equipment necessary to produce a crop.

A livestock producer cannot get his products to consumers without the agribusiness that processes those animals into cuts of meat to be sold at the retail level. I know as well as anyone that agri-*culture* cannot survive with agri-*business*. I do not believe my bill imposes an undue burden on agri-business.

I've heard it said that allowing USDA into the merger review process as my bills does "Politicizes" the process. But my legislation does not give USDA a rubber stamp to stop mergers. The only requirement that my bill places on USDA is for them to do a merger assessment based on a "Farmer-Impact" standard.

My bill encourages USDA to work with the merging parties to work out any concerns. It would do so without disrupting or displacing the process currently used by DOJ and FTC. And I emphasize: No merger can be stopped without a determination of an impartial Federal court that USDA has met the standard set by my legislation.

Bring USDA into the merger review process is not unprecedented. Currently, under a memo of understanding, USDA and DOJ consult and discuss with respect to AG mergers. My bill would formalize this process; make it more open and consistent. Furthermore, other agencies such as the Federal Communications Commission (FCC) and the Surface Transportation Board (STB) play integral roles in communications and railroad mergers, respectively. Giving USDA A prominent role in these reviews is not unprecedented.

It has also been implied that my bill would affect all business. I want to make it clear that my bill pertains only to agriculture. Agriculture concentration is one of the top issues that I hear about from producers in my State and agriculture is vital to my State's economy.

My bill would not drag the merger review process out; my bill requires USDA to conduct its farmer-impact assessment within the same time period as DOJ's merger review.

Because USDA represents farmers, my legislation guarantees farmers a place at the table when mergers in their industry are considered without making the process intolerably burdensome.

I want to reiterate my belief, Mr. Chairman, that my bill makes the AG merger review process more open and consistent in a way that is fair to both producers and agribusiness. I have said many times that I want to see meaningful action on Ag concentration taken in this Congress and I am committed to that goal.

Certainly, I believe there are ways in which my bill can be improved. And I am willing to listen to other's concerns and suggestions. But I will continue to push for congressional action on AG concentration so long as this Congress is in session.

This issue is too important to so many producers for it to be dropped. I know that many in the agribusiness community have been advocating a "Just say No" approach to AG concentration legislation. For me, and I believe other members, this do-nothing approach is not acceptable.

I urge the agribusiness community, who have worked with me on many occasions, to come to Congress with constructive proposals on how to guarantee AG producers that their concerns are heard when AG mergers are considered.

I want to commend Senator Daschle and Senator Leahy for their hard work and for bringing forward a substantive initiative. While there are differences between our bills, I believe there is enough common ground that we could reach a bipartisan agreement sooner rather than later.

Once again, I'D like to thank you, Mr. Chairman, for working as hard as you have to

help Congress understand AG concentration and what it means for America's farmers. I appreciate your willingness to put a great deal of time and effort into this issue and I look forward to working with you and the other members of the Committee to secure farmers' access to the marketplace.

Thank you.

Remarks by Senate Democratic Leader Tom Daschle
Hearing on Concentration in Agriculture
Senate Committee on Agriculture, Nutrition, and Forestry
April 27, 2000

Thank you, Mr. Chairman, for convening this hearing to discuss concentration and competition in the agriculture industry. I also want to thank the witnesses who are with us this morning. They all have very busy schedules, and many have come considerable distances, to share with us their insights into this crucial issue.

Earlier this month, I read an article in the New York Times. The headline was: "As life for Family Farmers Worsens, the Toughest Wither." Among all the pressures hammering at family farmers today, that article said, perhaps the most significant is the continuing industrialization of agriculture.

The month before that article appeared, there was another article -- this one in the Sioux Falls Argus Leader. The headline on that article read: "65% of Counties Lose Population." The Argus Leader story described the devastating effect of Smithfield Foods' purchase of the Dakota pork processing plant in Huron, South Dakota, a couple of years ago. Immediately after buying the plant, Smithfield closed it. Practically overnight the town lost 650 jobs – one-tenth of its entire work force. Less than a year later, pork prices fell to their lowest levels in decades. Pork processors attributed the drop to insufficient slaughter capacity.

Finally, I have a letter here from a member of the Kansas House of Representatives, who asks to remain nameless. In this letter, the writer describes an incident involving two of the "big four" packers. Based on the bids being offered over time, one of the packers apparently agreed to forfeit the market to the other. The letter writer goes on to explain that people harmed by this price collusion would not come forward because they feared retaliation by the packers. If they spoke out, the result, they feared, would be economic suicide for the entire feedlot. This is not an isolated case. I have heard other credible examples of this kind of unfair market manipulation. I suspect many of us have.

Over the past few years, we have all been presented with an abundance of evidence of the increasing market concentration in agriculture, and the terrible toll it is taking on producers and rural communities. We know that excessive market power increases the likelihood of anti-competitive behavior -- and the difficulty of preventing it. This is not a theory. This is not some hypothetical situation. It is happening – today – all across America. We have been warned repeatedly by industry experts and farm groups that we must act -- now -- to restore fair competition to agriculture -- and that, if we do not act, the markets will become increasingly inefficient, and rural America will be gravely harmed.

The bill my colleagues and I have introduced – S. 2411 -- *The Farmers and Ranchers Fair Competition Act of 2000,* will help restore fairness to agriculture markets by stimulating competition and increasing market participation by smaller, independent producers. It will do so in three specific ways. First, it will strengthen USDA's power to protect all producers from anti-

competitive practices. Second, it will require that the potential impact of proposed mergers on rural communities be considered during the process of reviewing proposed mergers. Third, our bill will restore fairness to agriculture markets by increasing the bargaining power of smaller, independent producers.

Our bill does not tar and feather agribusiness. It does not single out firms simply on the basis of size. And it does not construct a protective wall around any segment of the industry. What it does do is address the potentially negative consequences of agribusiness concentration. These include such things as: anti-competitive behavior by large producers; reduced market access for small producers; inadequate bargaining power; and economic depression in rural communities.

We are not trying to reshape the market. We are only trying to give farmers and ranchers the tools to succeed in this rapidly changing marketplace. Frankly, I would be comfortable going much further than we do in this bill. I think this crisis in rural America justifies an even tougher approach. But in the interest of making progress on this issue as soon as possible, Senator Leahy and I have sought to offer a middle way.

As the Committee knows, Senator Grassley also has introduced legislation on this subject. He has indicated interest in working on a bipartisan basis to achieve a solution. Senator Leahy and I, and the other cosponsors of S. 2411, appreciate his interest. We wholeheartedly support a constructive approach.

Mr. Chairman, small, independent farmers and ranchers deserve a fair chance to compete. But this bill is not simply about or for them. It is for all of us. We all benefit from the innovation and productivity generated by truly competitive markets. For the sake of family farmers and ranchers -- and for all Americans -- I am hopeful that we can pass legislation this year that will help restore fairness to the agricultural marketplace. I look forward to working with my colleagues to achieve that goal.

The Farmer and Rancher Fair Competition Act of 2000
(S. 2411)

1. Would strengthen laws prohibiting anti-competitive practices by broadening their scope to protect producers of all commodities, and adding provisions related to price discrimination, whistle blower protection, and limitations on the use of "right of first refusal" contract provisions

2. Would establish a 'Family Farmer and Rancher Claims Commission,' to provide compensation to producers for injury related to anti-competitive activities

3. Would expand the standard of review for mergers and acquisitions to include impacts on rural communities

4. Would establish minimum standards for marketing and production contracts, such as terms of duration, termination, renegotiation, and performance payments; responsibility for environmental damages and other local, state, or federal government compliance obligations; and use of plain language

5. Would prohibit confidentiality requirements that have the effect of preventing producers from seeking legal or financial counsel when deciding whether to sign a contract

6. Would require reporting of interlocking boards of directors and other inter-firm business relationships that may have implications for producer market-access, and bargaining power.

7. Would require appointment of a Special Counsel for Fair Markets and Rural Opportunity at USDA

8. Would require the General Accounting Office (GAO) reports on the following topics:
   - the competition-limiting effects of biotech patents and multinational mergers
   - the use of stock as the primary means of financing mergers and acquisitions
   - farm-to-retail price spreads
   - the impact of "right of first refusal" contract provisions on competitive opportunities for producers
   - market power related to formula contracts, marketing agreements, and forward contracting
   - the potential benefit of divestiture requirements
   - increased concentration in milk processing

STATEMENT OF SENATOR TIM JOHNSON

BEFORE THE

SENATE AGRICULTURE, NUTRITION, AND FORESTRY COMMITTEE

APRIL 27, 2000

PENDING LEGISLATION ON AGRICULTURAL BUSINESS CONCENTRATION

Thank you Mr. Chairman for conducting this vitally important hearing concerning ongoing agribusiness concentration in today's economy and pending legislation in Congress to address this critical matter.

As you know, I was joined earlier this year by Senators Grassley and Kerrey of this committee in a letter requesting your willingness to convene today's hearing. I am pleased you answered my call to discuss legislation I have introduced alongside others in this committee which seeks to ensure adequate competition in grain and livestock markets for family farmers and ranchers.

Furthermore, I want to thank you, Mr. Chairman, for the cooperation and leadership you exhibited last year in helping the Senate enact mandatory price reporting legislation. The work put forth by you and your staff within this committee to pass price reporting is greatly appreciated. South Dakota's livestock producers should take great pride in the fact they were largely responsible for the passage of mandatory price reporting legislation last year. South Dakota became the first state in the nation to implement a price reporting law during their 1999 Legislative Session, prompting other states (Nebraska, Minnesota, Iowa, and Missouri), and eventually Congress, to follow suit. Passage of price reporting legislation is a substantial first step towards restoring confidence in the livestock market.

However, much more must be done to make the marketplace free and fair for independent farmers and ranchers.

Concentration Putting a Squeeze on an Open Marketplace in the United States
Last fall, the largest hog processor in the nation, Smithfield Foods, announced their intentions to own all the hogs currently held by both Murphy Farms and the Tyson Pork Group, effectively eliminating the need for Smithfield to buy from independent producers. These proposed actions would also make Smithfield the nation's top hog producer. While the Smithfield / Tyson deal is now defunct, Smithfield still plans to move ahead with its acquisition of Murphy Farm's hogs.

Within the last few days, Smithfield Foods - which indeed now is the country's largest processor and producer of hogs - purchased and subsequently shut down a hog processing plant in Dubuque, Iowa. South Dakota pork producers are particularly sensitive to this action because in the summer of 1997, Smithfield did the exact same thing to a pork plant in Huron, South Dakota. The very recent arm flexing tactics of this company continues to eliminate markets for independent pork producers, especially in the Northern Plains.

Concentration in agriculture leads to a marketplace where a small number of firms control agricultural goods between producers and consumers. These firms then leverage a dominating

amount of bargaining power over both producers and consumers. Overzealous horizontal concentration has left the U.S. with three or four big meatpackers left to purchase beef cattle, pork, and lamb for slaughter. Subsequent vertical integration by some of these same horizontally concentrated firms has left the open marketplace, a keystone component of our free enterprise system, in serious jeopardy.

Yet, that open marketplace is still the major price discovery mechanism that independent producers rely upon. So, when the open market is thin (lacking activity), the ability of one or two dominant marketplace players to affect the market is tremendous. For instance, if in a given week a meatpacker utilizes all of its captive supplies and packer owned livestock to fill its kill needs, it has the ability to level off a price spike or even depress prices paid in the open market.

I would like to discuss this practice of packer ownership of livestock in greater detail because I have introduced legislation to forbid this sometimes manipulative procurement practice.

Packer Ownership of Livestock Effects the Marketplace

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

According to Dr. Ron Plain, agricultural economist at the University of Missouri, 75 percent of hogs are either packer-owned or under production contracts by packers. Other studies and estimates indicate at least nearly 60 percent of the slaughter market for hogs is under packer ownership and control. With the Smithfield actions yet to take their toll on the marketplace, no one really knows to what degree the hog slaughter market is controlled by captive supply and packer ownership.

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

Independent cattle feeders and farmers used to have several buyers competing for their cattle every day of the week. With increasing captive supplies, packers do not bid aggressively for cattle to fill their slaughtering needs. In some instances, cattle feeders have only a few hours within one or two days a week to accept packer bids for cattle, most often in "take it or leave it" scenarios.

Economists consulting the Western Organization of Resource Councils found that for each percent of captive supply, spot or cash prices decreased by eight cents per hundred weight.

The RANCHER ACT (S. 1738) Addressing Packer Ownership of Livestock

I have introduced legislation to rein in the meatpackers' leverage over the livestock market and reestablish a free, fair, and competitive atmosphere for independent livestock producers. I have been joined by Senators Kerrey (D-NE), Grassley (R-IA), Thomas (R-WY), Daschle (D-SD), Harkin (D-IA), Dorgan (D-ND), Wellstone (D-MN), Conrad (D-ND), and Bingaman (D-NM) in introducing S. 1738 (the RANCHER Act) to prohibit meatpackers from owning livestock prior to slaughter. Reps. Minge (D-MN) and Leach (R-IA) have introduced similar legislation in the

House of Representatives.

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

My legislation is timely because of recent movement in the meatpacking industry, movement to choke-off market access from independent livestock producers.

My bill recognizes the need for greater value-added opportunities and exempts producer owned and controlled cooperatives and small producer owned meatpackers from the ownership prohibition. This legislation is also retroactive - requiring meatpackers to divest of ownership interests in livestock - which directly takes on the potential Smithfield deals.

A recent survey of over 1000 farmer-members of the Iowa Pork Producers Association found that 88 percent support a federal level ban of packer ownership of hogs.

Elected leaders serving in the state legislatures of South Dakota and Iowa have taken steps to let livestock producers know they support erasing anticompetitive behavior in the marketplace, and they have been catalysts for change on this issue. In South Dakota, Governor Janklow signed a resolution adopted by the legislature calling for a federal level prohibition of packer ownership of livestock. And in Iowa, legislation was passed to strengthen their existing law on packer ownership, and Governor Vilsack signed this provision into law just recently.

Finally, nearly 3000 farmers, ranchers, clergy, and rural business people participating in the Rally for Rural America placed a high priority on Congressional action to forbid meatpacker ownership of livestock when they journeyed to the nation's capital in March of this year.

A ban on packer ownership of livestock would not drive packers out of business. As indicated in earnings reports and press releases from the major packers, most of their income and earnings are generated from branded products and companies marketing products in a more direct fashion to consumers.

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

Why are my colleagues and I so concerned about packer ownership of livestock? We already know growing packer concentration creates an imbalance in bargaining power between a few meatpackers who buy livestock and several producers who sell livestock. The relative lack of buyers means the buying side of the market has much more power than the selling side.

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

As a consequence of having slaughter livestock supplies locked up through captive supplies, meatpackers do not have to bid competitively for all of their slaughter needs. This may depress the marketplace and restrict access to producers and feeders without the arrangements.

Moreover, packer ownership of livestock increases the likelihood of price manipulation in the marketplace. When packers own livestock, they have the ability to push forward or hold back captive supplies in response to market price.

Some have criticized my efforts to keep meatpackers from owning livestock, but given a choice, I will side with a broad base of family farmers and ranchers over conglomerate agriculture any day. It boils down to whether we want independent producers in agriculture, or if we will yield to concentration and see farmers and ranchers become low wage employees on their own land.

Farmers and Ranchers Fair Competition Act of 2000 (S. 2411)
I am also very pleased to join Senator Daschle and twelve other Senators in introducing a comprehensive bill - S. 2411 - that takes on anticompetitive issues in agriculture today. This legislation compliments my legislation to ban packer ownership.

S. 2411 recognizes the role that three government agencies have over competition policy in agriculture today. The Federal Trade Commission (FTC) and Department of Justice (DOJ) deal with antitrust matters in agriculture and other industries. In addition, USDA's Grain Inspection, Packers and Stockyards Administration (GIPSA) handles anticompetitive practices in meatpacking. This legislation seeks better cooperation and communication among DOJ and USDA among many other things.

I want to mention three principal provisions of this legislation. First, S. 2411 clarifies that meatpackers and others engaging in unjustifiable price discrimination and preferential purchasing are violating the law. Too many farmers and ranchers feel agribusiness buyers have discriminated against them based on the size of their operations, so our bill clearly prohibits these practices. Our bill restates and bolsters some of the prohibitions listed in the Packers and Stockyards Act of 1921. In addition, if farmers and ranchers are economically harmed by anticompetitive behavior, our bill establishes a "Family Farmer and Rancher Claims Commission" authorized to direct compensation to them.

Second, the bill requires USDA analysis of proposed agribusiness mergers to determine if a given merger will have a negative effect on family farmers, market prices, and rural communities. It is necessary for USDA to have a role in this process.

Third, since many producers are either coerced or attracted into contract production scenarios, I am pleased the bill requires basic public disclosure standards for these contracts. A producer needs to know if the contract he/she is signing is worth the paper it is written on. Poultry producers learned the hard way that some contracts are recipes for disaster to the independent farmer.

Finally in regards to livestock markets, I would like to mention three legislative initiatives related to fair and free competition in the marketplace that I support and encourage Congress to act upon this year.

Country-of-Origin Meat Labeling
First, I continue to push for legislation to require country-of-origin labeling for meat products. Fifteen Senators have co-sponsored my bill, S. 242 (the Meat Labeling Act of 1999), including Senator Baucus (D-MT), Senator Daschle (D-SD), Senator Grassley (R-IA), Senator Harkin (D-IA), Senator Kerrey (D-NE), Senator Conrad (D-ND), Senator Bingaman (D-NM), Senator Bond (R-MO), Senator Campbell (R-CO), Senator Durbin (D-IL), Senator Enzi (R-WY), Senator Feingold (D-WI), Senator Graham (D-FL), Senator Reid (D-NV), and Senator Thomas (R-WY). The bill will require country-of-origin labeling for muscle cuts and ground products of beef, lamb, and pork.

The results of a study conducted by Wirthlin Worldwide in March of 1999 indicated that 91% of the consumers surveyed said that if given the choice between a U.S. meat product and that from another country, they would choose the U.S. meat. It should be noted that both the EU and Japan plan to implement country-of-origin meat labeling this year (in 2000).

USDA Quality Grade Reform

Second, I have also introduced S. 241, (the Truth in Quality Grading Act of 1999). This bill prohibits imported beef and lamb from displaying USDA quality grade stamps. Foreign meat products now enjoy the use of the USDA quality grade as a marketing tool. Too often, foreign nations mask their meat products under the USDA quality grade which misleads some consumers to believe the USDA grade means the meat product is from the United States. USDA recently solicited public opinion concerning whether the Secretary should use administrative authority to discontinue using USDA quality grades on imported beef and lamb meat carcasses. I believe this is a step in the right direction, although my legislation is more comprehensive, and I look forward to working with USDA to remedy this matter quickly.

Interstate Shipment of Meat

Finally, I recently joined Senator Daschle and many others in cosponsoring S. 1988 (the New Markets for State Inspected Meat Act). This legislation will permit the interstate shipment of state inspected meat. The bill has been endorsed by USDA, major farm organizations, and consumer groups.

Thank you for holding this very important hearing today Mr. Chairman.

Agricultural Concentration and Competition Hearing
Statement of Senator Bob Kerrey
4/27/00

Mr Chairman, thank you for holding this hearing today. Concentration is one of the most important issues facing the agriculture industry today, and I am pleased that the Senate Agriculture Committee is paying attention to this problem. Our farmers and ranchers have been saying it for years -- the increase in mega-mergers and consolidation in agriculture has resulted in concentration of power in the hands of a few. The results have very human consequences: the depopulation of rural America; the closing of schools and hospitals; the burden of moving rural residents to cities; and the loss of people produced on farms. We all recognize that there is a public good to family-based agriculture, just as there is public good to child labor laws.

I am frustrated, however, that Congress has been unable to respond to what people are saying. I hope to push through legislation yet this year to combat concentration within agriculture. I am pleased to be a cosponsor of S. 2411, the Farmers and Ranchers Fair Competition Act of 2000 that Senators Daschle and Leahy have introduced. This bill will strengthen USDA's ability to protect producers from anti-competitive practices and creates a role for USDA in merger reviews. The concentration of power in the hands of a few can increase the likelihood that farmers or ranchers will be the victim of unfair or deceptive practices. This bill gives USDA the authority to help address those practices.

Senator Johnson and I have also introduced S. 1738, the RANCHER Act, to prohibit packer ownership of livestock. Our bill will help insure competitiveness in the livestock industries. This bill prohibits meatpackers from owning, feeding, or keeping livestock for more than 14 days prior to slaughter. It does exempt producer-owned and -controlled co-ops and small producer-owned meatpackers from the ownership prohibition. There is a great deal of concern in Nebraska about vertical integration of livestock industries. In fact, packer ownership is already illegal in Nebraska. This bill would take Nebraska's good judgment to the rest of the country.

Some national agriculture groups have spoken out against these anti-concentration bills, but I think it is important to note that many of the state organizations in my region, those groups closest to our farmers and ranchers, have signaled that they believe packers should not be able to own livestock. Recently, Nebraska Pork Producers (as well as Iowa, Michigan and Wisconsin Pork Producers) submitted proposals to the National Pork Forum to prohibit packer ownership of hogs.

Mr. Chairman, I thank you again for conducting this hearing, and I reiterate my strong desire to take action on concentration in the agriculture industries before Congress adjourns for the year.

Department of Justice

STATEMENT

OF

JOHN M. NANNES
DEPUTY ASSISTANT ATTORNEY GENERAL
ANTITRUST DIVISION

BEFORE THE

COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY
UNITED STATES SENATE

CONCERNING

ANTITRUST ENFORCEMENT IN AGRICULTURE

PRESENTED ON

APRIL 27, 2000

I am pleased to have the opportunity this morning to discuss issues relating to antitrust enforcement in the agricultural marketplace.

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

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

The Antitrust Division takes these concerns seriously and has been very active in enforcing the antitrust laws in the agricultural sector. During the past two years alone, the Antitrust Division has challenged a number of significant mergers that would have affected agricultural markets, such as:

- the proposed acquisition by Monsanto of DeKalb Genetics

Corporation, which would have significantly reduced competition in corn seed biotechnology innovation to the detriment of farmers;

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

During the same period, the Antitrust Division also criminally prosecuted companies that had fixed prices for products purchased by farmers -- lysine and vitamins -- and secured numerous criminal convictions and the highest fines in antitrust history.

These enforcement actions demonstrate that the Antitrust Division is committed to enforcing the antitrust laws in the agricultural marketplace.

I. Merger Enforcement

In our conversations with farm groups, we have found that farmers are especially concerned about the potential impact of mergers and acquisitions ("mergers"). Farmers are concerned that mergers will limit the number of sellers of seed, chemicals, machinery, and other equipment from whom they have to buy

and will limit the number of customers for crops and livestock to whom they can sell. For this reason, I think it may be helpful today to start with a discussion of the Antitrust Division's merger enforcement program, with particular emphasis on recent merger enforcement actions that the Antitrust Division has taken in the agricultural sector.

A. Merger Enforcement Standards

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

The Antitrust Division shares merger enforcement responsibility with the Federal Trade Commission ("FTC"), with the exception of certain industries in which the FTC's jurisdiction is limited by statute. The agencies jointly have developed Horizontal Merger Guidelines that describe the inquiry they will follow in analyzing mergers. "The unifying theme of the Guidelines is that mergers

should not be permitted to create or enhance market power or to facilitate its exercise. Market power to a seller is the ability profitably to maintain prices above competitive levels for a significant period of time." Merger Guidelines § 0.1.

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

In most instances, the Antitrust Division is concerned about the ability of the merging companies to raise above the competitive level the price of the products or services they sell. Of course, it is also possible that a merger will substantially lessen competition with respect to the price that the merging companies pay to purchase products. This is a matter of particular concern to

farmers, who often sell their products to large agribusinesses. For a while, there seems to have been some uncertainty about whether the antitrust enforcement agencies take this possibility into account when analyzing mergers. In fact, the Merger Guidelines specifically provide that the same analytical framework used to analyze the "sell-side" will be applied to the "buy-side":

> Market power also encompasses the ability of a single buyer (a "monopsonist"), a coordinating group of buyers, or a single buyer, not a monopsonist, to depress the price paid for a product to a level that is below the competitive price and thereby depress output. The exercise of market power by buyers ("monopsony power") has adverse effects comparable to those associated with the exercise of market power by sellers. In order to assess potential monopsony concerns, the Agency will apply an analytical framework analogous to the framework of these Guidelines.

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

While most of the mergers that the agencies review involve horizontal competitors, the agencies also have guidelines on non-horizontal mergers that address the circumstances in which a vertical merger -- a transaction between companies at different levels in the production and marketing process -- may be

challenged.

B. Procedures for Reviewing Mergers

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

We take concentration into account even at this very early stage of our review. In determining whether or not to conduct an investigation, we consider the pre-merger and post-merger concentration level in the affected markets. In those industries already characterized by high concentration levels, there is a substantially increased likelihood that a proposed merger will be subject to a formal -- and often quite extensive -- antitrust investigation.

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

antitrust agency has other statutory powers for obtaining information.

If the reviewing antitrust agency concludes that the merger is not competitively problematic, the investigation will end and the parties then are generally free to proceed with the merger. However, if the reviewing antitrust agency does not fully resolve its competitive concerns, the agency will identify the nature of its competitive concerns and the parties will have an opportunity to address them. Unless the parties can convince the agency that suit is not warranted, the agency will prepare to file suit to challenge the transaction as originally proposed. Sometimes the parties make a proposal to address the competitive concerns that the reviewing antitrust agency has identified; for example, a merger between multi-product firms may raise competitive concerns with respect to only a subset of their products, in which case divestiture may solve the competitive problem, allowing the parties to proceed with the rest of the merger. There are times, however, when the merging parties' proposed changes to the merger are not enough to solve the problem, in which case the reviewing antitrust agency will challenge the merger and likely seek a preliminary injunction to prevent consummation of the merger while it is being challenged.

C. Recent Merger Enforcement Actions in Agricultural Industries

As a result of the clearance process with the FTC, the Antitrust Division has investigated the preponderance of mergers affecting agriculture, with a prominent exception being grocery store mergers, which are usually reviewed by the FTC. In the past two years, the Antitrust Division has objected to four significant proposed mergers in agriculture-related industries that we concluded would adversely affect farmers. Each of those transactions was important in its own right, and collectively they demonstrate the Antitrust Division's commitment to enforce the antitrust laws in this vital segment of our economy.

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

create their own corn hybrids.

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

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

wheat and corn from farmers in central California; and (3) Beaumont, Texas, where the elevators competed to purchase soybeans and wheat from farmers in east Texas and western Louisiana.

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

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

This relief assures that farmers in the affected markets will continue to have alternative buyers to whom to sell their grain and soybeans. The case

demonstrates that the Antitrust Division will challenge mergers that threaten competitive harm to sellers of goods and services.

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

The parties agreed to significant divestitures in order to address our concerns. Those divestitures included New Holland's large two-wheel-drive agricultural tractor business, New Holland's four-wheel-drive tractor business, and Case's interest in a joint venture that makes hay and forage equipment.

4. Most recently, Monsanto abandoned its proposed acquisition of Delta & Pine Land Co., after the Antitrust Division indicated that it was prepared to sue to prevent consummation of the transaction. The Antitrust Division concluded that

the merger, which would have combined the two largest cotton seed companies, would have anticompetitively harmed farmers raising cotton.

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

II. Criminal Enforcement of the Antitrust Laws

In addition to our merger enforcement program, the Antitrust Division has moved aggressively to prosecute companies that engage in price fixing or

allocation of customers. Such conduct willfully subverts the operation of free markets and can cause serious economic harm. It virtually always results in inflated prices to purchasers or depressed prices to suppliers; indeed, that is the very purpose of such conduct.

The key to such illegal conduct is an agreement among competitors. It is not enough for us to show that competitors charged the same or similar prices for a product or service. The Antitrust Division must prove that the competitors agreed upon prices or price levels, or upon the allocation of customers or markets, although we may be able to rely upon circumstantial evidence in order to do so. A company convicted of violating the antitrust laws is subject to substantial fines, and an individual convicted of violating the antitrust laws is subject to fine and imprisonment.

In the past few years, the Antitrust Division has prosecuted a number of cases and secured convictions and multi-hundred million dollar fines in various industries that have involved products purchased by farmers. Two prosecutions deserve particular mention.

1. Beginning in 1996, the Antitrust Division prosecuted Archer Daniels Midland and others for participating in an international cartel organized to suppress competition for lysine, an important livestock and poultry feed additive.

The cartel had inflated the price of this important agricultural input by tens of millions of dollars during the course of the conspiracy. ADM pled guilty and was fined $100 million -- at the time the largest criminal antitrust fine in history. Two Japanese and two Korean firms also were prosecuted for their participation in the worldwide lysine cartel and were assessed multi-million dollar fines. In addition, three former ADM executives were convicted for their personal roles in the cartel; two of them were sentenced last year to serve two years in prison and fined $350,000 apiece for their involvement, and the other executive had 20 months added to a prison sentence he was already serving for another offense.

2. Last year, the Antitrust Division prosecuted the Swiss pharmaceutical giant, F. Hoffmann-La Roche Ltd., and a German firm, BASF Aktiengesellschaft, for their roles in a decade-long worldwide conspiracy to fix prices and allocate sales volumes for vitamins used as food and animal feed additives and nutritional supplements. The vitamin conspiracy affected billions of dollars of U.S. commerce. Hoffman-La Roche and BASF pled guilty and were fined $500 million and $225 million, respectively. These are the largest and second-largest antitrust fines in history -- in fact, the $500 million fine is the largest criminal fine ever imposed in any Justice Department proceeding under any statute. Three former Hoffmann-La Roche executives from Switzerland and three former BASF

executives from Germany agreed to submit to U.S. jurisdiction, to plead guilty, to serve time in a U.S. prison, and to pay substantial fines for their role in the vitamin cartel. These prosecutions are part of an ongoing investigation of the worldwide vitamin industry, in which there have been 18 prosecutions to date.

The Antitrust Division will prosecute companies for price fixing whenever and however we learn of it. The lysine and vitamin cases get publicity because of the prominence of the companies involved and the amount of commerce at stake, but we also successfully prosecuted two cattle buyers in Nebraska a few years ago for bid-rigging in connection with procurement of cattle for a meat packer, after an investigation conducted with valuable assistance from the Department of Agriculture, which was investigating some of the same conduct under the Packers and Stockyards Act. In short, we have brought -- and will continue to bring -- charges against companies that engage in criminal behavior that adversely affects farmers.

III. Other Potential Anticompetitive Conduct

The Antitrust Division also investigates other forms of business behavior that may have anticompetitive effects. Such conduct may constitute an illegal restraint of trade or unlawful monopolization or attempted monopolization. Conduct that may raise competitive issues of particular interest to farmers include

strategic alliances between agribusiness companies, joint ventures among suppliers, and misuse of intellectual property rights.

The Antitrust Division is conducting a number of civil investigations in which we are considering whether conduct is having an anticompetitive impact upon farmers. It we determine that such is the case, we can and will seek appropriate relief under the antitrust laws.

IV. Additional Steps to Ensure Appropriate Antitrust Enforcement

The Antitrust Division has taken additional steps to assure that it is receiving the information necessary to make the best-informed judgments with respect to agricultural antitrust issues.

Last year, the Antitrust Division (and the FTC) entered into a memorandum of understanding with the Department of Agriculture to assure that the agencies would continue to work together and exchange information relating to competitive developments in the agricultural marketplace. As part of this cooperation, the Department of Agriculture has provided significant assistance and expertise in the various agricultural industries that have been the focus of investigation. The Antitrust Division also works with other relevant federal agencies on specific matters of common interest. For example, the Antitrust Division worked closely with the Commodities Futures Trading Commission during the investigation of the

Cargill/Continental merger.

Finally, earlier this year, Assistant Attorney General Joel Klein appointed Doug Ross as special counsel for agriculture. This is a newly created position that reports directly to the Assistant Attorney General. In this position, he is assigned to work exclusively on agricultural issues. He has over 25 years of law enforcement experience, both in and outside the Antitrust Division, and has already begun to meet and speak with farm groups both here in Washington and in farm states. Among his particular qualifications for the position is his long-time association with the National Association of Attorneys General. The Antitrust Division has often worked with state attorneys general in trying to ascertain the potential impact of agricultural transactions on local farmers, and his assignment to agricultural matters on a full-time basis ensures that this process will be intensified.

V. Conclusion

Mr. Chairman and members of the Committee, the Antitrust Division understands the concerns that have been expressed about competition in agricultural markets. We take seriously our responsibility to assure that the antitrust laws are enforced no less vigorously in agricultural markets than in other markets to which those same laws apply. We believe that our record of antitrust

enforcement in this important sector of the economy demonstrates that commitment.

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

STATEMENT OF JAMES F. RILL
BEFORE THE COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY
U.S. SENATE

Regarding Concentration in Agribusiness and Legislative Proposals to Provide the U.S. Department of Agriculture With Oversight Powers in the Review of Competition-Related Aspects of Agribusiness Mergers

April 27, 2000

Mr. Chairman and members of the Committee, my name is James F. Rill, and I am testifying this morning on behalf of the Industry Structure Coalition, a broad group of agricultural, food and other trade associations, which opposes S. 2252 and S. 2411.[1] I appreciate the opportunity to participate in these hearings and to offer my thoughts on the proposed legislation regarding agribusiness concentration and competition issues. The focus of my testimony will be solely on the merger-related aspects of the proposed legislation. The views expressed today are my own.

I. SUMMARY OF TESTIMONY

Several bills have been introduced to address the so-called "merger-mania" that is

[1] The Coalition's members include the American Bakers Association, American Crop Protection Association, American Feed Industry Association, American Meat Institute, Animal Health Institute, Food Distributors International, Grocery Manufacturers of America, International Dairy Foods Association, National Association of Manufacturers, National Chicken Council, National Fisheries Institute, National Food Processors Association, National Grain Trade Council, National Turkey Federation, North American Meat Processors Association, North American Millers Association, Snack Food Association, The Fertilizer Institute, and the Transportation, Elevator and Grain Merchants Association.

spreading through the agriculture sector of the nation's economy.[2] Two of these bills, S. 2252 and S. 2411, authorize the U.S. Department of Agriculture ("USDA") to challenge agribusiness mergers. I believe that these bills are unnecessary and potentially detrimental for several reasons. First, as a general matter, it is problematic for the antitrust enforcement agencies and sectoral regulators to exercise concurrent authority to challenge the competition-related aspects of proposed mergers. Such dual jurisdiction undercuts the critical goal of ensuring that competition policy and procedures in this country are consistent and coherent. This view is reflected in a comprehensive report issued by the International Competition Policy Advisory Committee, a Committee comprised of members from business, academia and law, for which I served as Co-Chair. Second, the U.S. Department of Justice ("DOJ") and the Federal Trade Commission ("FTC") aggressively enforce the antitrust laws in the context of agribusiness consolidation. These enforcement agencies have institutional expertise in agriculture and competition issues, as well as rely on a variety of external sources for industry expertise and advice, including the USDA. Third, the antitrust principles applied by the DOJ and FTC in the merger context fully and fairly consider competition issues in the agricultural sector, including the effect of a proposed merger on family farmers.

II. RELEVANT HIGHLIGHTS OF LEGISLATIVE PROPOSALS

Since I am confining my testimony today to the merger aspects of the proposed legislation, I will briefly touch on those provisions of each bill. S. 2252, known as the "Agriculture Competition Enhancement Act," provides the U.S. Department of Agriculture

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[2] Statements on Introduced Bills and Joint Resolutions, Cong. Rec. S1464 (statement by Senator Grassley regarding S. 2252) (Mar. 20, 2000).

("USDA" or the "Department") the authority to challenge an agribusiness acquisition or merger if the Department believes the transaction would cause "substantial harm" to the ability of "independent producers and family farmers" to compete in the marketplace. The bill also calls for the creation of a Special Counsel for Competition Matters within the USDA whose primary responsibility would be to analyze mergers and acquisitions in the food and agriculture sectors in consultation with the USDA's Chief Economist. Factors that the Special Counsel would consider when reviewing a merger or acquisition include: (1) the effect of the transaction on prices paid to producers who do business with one or more of the parties; (2) the likelihood that the transaction would significantly increase market power for the new surviving entity; (3) the likelihood that the transaction would increase the potential for anticompetitive conduct by the new surviving entity; and (4) whether the transaction would adversely affect producers in a particular region, including an area as small as a single state.

S. 2411, the "Farmers and Ranchers Fair Competition Act of 2000," empowers the Secretary of Agriculture to review large agribusiness mergers and acquisitions to determine whether a proposed transaction "could" lead to unfair practices as defined in the bill, or could be "significantly detrimental to the present or future viability of family farms or ranches or rural communities" in the affected areas. The Secretary may issue a report to the parties of the proposed transaction, outlining an approach that would likely avoid the alleged unfair practices or alleged detrimental impact of the merger. If, however, the parties fail to institute the Secretary's recommended or otherwise agreed upon approach to resolving the alleged problems with the transaction, the Secretary shall consider the transaction to be unlawful under Section 4

of the bill and the Secretary may assess civil penalties against the parties.[3]

III. THE ICPAC REPORT STRONGLY DISFAVORS CONCURRENT REVIEWS OF MERGERS BY ANTITRUST AND SECTORAL AGENCIES

In November 1997, Attorney General Janet Reno and Assistant Attorney General Joel Klein announced the formation of the International Competition Policy Advisory Committee ("Advisory Committee") to study and present recommendations to the Justice Department on the future of international antitrust policy. The Committee's mandate focused on three specific areas: (1) multijurisdictional merger review, (2) the interface between trade and competition policy, and (3) cooperation in the prosecution of international cartel activity. The Advisory Committee, of which I was privileged to serve as Co-Chair, was composed of members from varied backgrounds, including business, academia, and law.[4] Over the course of its existence, the Advisory Committee heard from a wide range of experts and enforcement officials on a myriad of issues pertaining to increasing globalization and the role of antitrust on that stage. The Advisory Committee issued its Final Report on February 28, 2000, which consisted of more than 300 pages and numerous recommendations to both the United States' antitrust agencies as well as competition officials worldwide.

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[3] Section 4 of S. 2411 makes it unlawful for a dealer, processor, commission merchant, or broker to, *inter alia*, engage in or use any unfair, unreasonable, unjustly discriminatory, or deceptive practice or device in the marketing, receiving, purchasing, sale, or contracting for the production of any agriculture commodity. If the Secretary of Agriculture has reason to believe that a violation of any of these prohibitions has occurred, the Secretary is authorized to issue complaints, hold hearings, issue subpoenas, issue cease and desist orders, and assess civil penalties. The Secretary may also sue for temporary injunctions.

[4] A complete list of the Advisory Committee members is attached to this testimony.

The Advisory Committee's Concerns With Multiple Agencies Reviewing Competitive Aspects of Mergers

One of the issues addressed by the Advisory Committee in its Final Report was the existence within the United States of dual review of mergers by both antitrust agencies and sectoral regulatory agencies.[5] The majority of Advisory Committee members recommended removing the oversight authority for competition-related aspects of merger review from the sectoral agencies, such as the Federal Communications Commission ("FCC") and the Surface Transportation Board ("STB"), and vesting such power exclusively in the federal antitrust agencies.[6] While sectoral regulatory agencies would still maintain authority over non-competition related issues, conclusions of the Department of Justice and the FTC would be binding insofar as the competitive merger review analysis.

The Advisory Committee's recommendation stemmed from its concerns regarding the inherent duplication and inefficiencies encountered during multiple reviews by different agencies. Such multiple merger reviews impose significant costs on industry participants through the need to respond to and defend the competition-related aspects of a single transaction before more than one agency and generate increased uncertainty as standards and time frames for

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[5] The debate and discussion which occurred within the Advisory Committee was assisted in large part by a paper prepared for the Advisory Committee by William E. Kovacic, "The Impact of Domestic Institutional Complexity on the Development of International Competition Policy Standards," (Mar. 15, 1999).

[6] A minority of Advisory Committee members instead recommended creating a presumption in favor of the competition-related analyses of the antitrust enforcement agencies in the merger review process.

the review process often differ between agencies.[7] Similarly, dual jurisdiction promotes inefficient allocation of scarce agency resources through often duplicative competitive analyses and instances in which the comparative advantage of antitrust agencies is not utilized to its fullest extent. In addition to the costs imposed on both business and federal regulators, multiple review of mergers also hinders the ability to create consistent competition-based standards and policies, as well as contributing to a lack of transparency in the procedural aspects of merger review. Finally, the Advisory Committee expressed concern that the existence of such domestic overlapping jurisdiction of mergers could undercut international efforts to establish harmonization of policies and cross-border cooperation. In this regard, a perception may be created that the FTC and Justice Department cannot communicate definitively with a foreign government about a particular transaction because their views would not necessarily be binding following the merger review process by a sectoral agency.

Some Sectoral Agency Officials With Merger Review Authority Have Questioned The Necessity of Dual Merger Review Jurisdiction

In addition to the recommendations incorporated in the Advisory Committee's Final Report, several sectoral agency officials with merger review authority recently have recommended eliminating dual merger review jurisdiction based on many of these identical concerns. Specifically, FCC Commissioners Michael Powell and Harold Furchtgott-Roth have publicly expressed concern regarding the dual jurisdiction of the FCC and Antitrust Division over telecommunications mergers. Following the FCC approval of the WorldCom/MCI

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[7] *See also* James F. Rill, et al., *Institutional Responsibilities Affecting Competition in the Telecommunications Industry: A Lawyer's Perspective*, European University Institute, 1998 EU Competition Workshop, at 24.

transaction, Commissioner Powell noted in a separate statement that the FCC should attempt to concentrate its efforts on issues relevant to its own expertise, instead of a competition-based analysis undertaken by the Antitrust Division.[8] This sentiment was expressed further by Commissioner Furchtgott-Roth when he stated that the FCC has "little to add or to subtract from the market analyses" performed by the DOJ.[9] More recently, both Commissioners Powell and Furchtgott-Roth endorsed portions of the Advisory Committee's Final Report on this issue in legislative testimony.[10] In addition, Commissioner Curt Hébert of the Federal Energy Regulatory Commission ("FERC") favorably noted the Advisory Committee's conclusions in a speech where he argues for the elimination of merger review authority for FERC.[11]

Application Of Concerns Regarding Dual Merger Review To Proposal Giving USDA Merger Review Authority Over Agribusiness Mergers

While not specifically addressed in the Advisory Committee's Final Report, the pending legislation that proposes extending antitrust merger review authority to the USDA implicates

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[8] Separate Statement of FCC Commissioner Michael Powell Regarding the Application of WorldCom, Inc. and MCI Telecommunications Corp., CC Dkt. No. 97-211, at 4 (Sept. 14, 1998).

[9] Separate Statement of Commissioner Harold Furchtgott-Roth Regarding the Application of WorldCom, Inc. and MCI Telecommunications Corp., CC Dkt. No. 97-211, at 1 (Sept. 14, 1998) (also suggesting that multiple merger review contributes to the length of the entire merger review process).

[10] *See* Prepared Statement of The Honorable Michael K. Powell, Before the U.S. House of Representatives Subcommittee on Telecommunications, Trade, and Consumer Protection, at n. 6 (Mar. 14, 2000); Prepared Statement of The Honorable Harold Furchtgott-Roth, Before the U.S. House of Representatives Subcommittee on Telecommunications, Trade, and Consumer Protection, at 2 (Mar. 14, 2000).

[11] Remarks by Commission Curt Hébert on FERC's Role in Merger Review, Washington, D.C. (Mar. 15, 2000).

many of the concerns of overlapping merger review discussed above and would appear to contradict the recommendations expressed in the Advisory Committee's Final Report. Antitrust merger review authority for agribusiness mergers is currently vested primarily in the federal antitrust agencies. By extending that jurisdiction to another agency, the USDA, the potential for duplication and inefficient use of resources subsequently increases. Transaction costs for the agribusiness community would increase as parties would be forced to respond to potentially duplicative requests and investigations from multiple agencies on the competitive effects of a proposed combination. Additionally, as the Advisory Committee's Final Report notes, domestic multiplicity undercuts international efforts to streamline the worldwide review of transactions. If the United States introduces additional levels of review, it might provide implicit encouragement for foreign antitrust authorities to establish a similar regime (*e.g,* the EU might permit each member nation to review all mergers among United States companies for their impact on the farmers of each member nation). The pending legislation at issue holds the potential to increase the burden on business, create duplicative responsibilities for federal enforcement agencies thereby wasting valuable and limited resources, and generate a less transparent environment – while current review of the competition aspects in agribusiness mergers are being effectively addressed by the federal antitrust agencies.

V. THE CURRENT APPROACH TO AGRIBUSINESS MERGER REVIEW WORKS EFFECTIVELY TO ENSURE A FULL AND FAIR EXAMINATION OF COMPETITION ISSUES, INCLUDING THE EFFECT OF A PROPOSED MERGER ON FAMILY FARMERS

The process by which the antitrust enforcement agencies investigate proposed agribusiness mergers includes consultation with USDA , as well as academics, business people,

economists and others with a strong breadth and depth of expertise in the agriculture industry and competition issues. Moreover, the antitrust legal standards applied by the antitrust enforcement agencies for almost a century provide a fair and consistent approach to agribusiness merger review, which includes comprehensive consideration of the effect of a proposed agribusiness merger on family farmers. Further, the proposed bills delineate different and vague standards from those embodied in the antitrust laws, thereby severely undercutting the critical goal of ensuring that U.S. competition policy standards and procedures are consistent and cohesive.

The Antitrust Agencies' Current Approach to Agribusiness Merger Investigations Incorporates Extensive Expertise in Agriculture Issues

The DOJ and the FTC share merger enforcement responsibility. These two antitrust enforcement agencies use a clearance process to determine which agency will review a particular merger, with the primary consideration being which agency has expertise about the products or services at issue in the proposed transaction. In recent years, many of the agribusiness transactions have gone to the Transportation, Energy & Agriculture Section of the DOJ, a section, which as the name indicates, has particular expertise in the agriculture sector. In 1999, Assistant Attorney General Joel Klein established within the Division the new position of Special Counsel for Agriculture. The Special Counsel focuses full-time on the agricultural marketplace and provides assistance and advice to supplement the Division's ongoing antitrust enforcement efforts in agribusiness consolidation matters.

Further expertise is provided to the DOJ from the USDA and other agencies involved with agriculture issues. In the DOJ's investigation of the Cargill/Continental Grain merger, the

DOJ relied on valuable assistance from the USDA, the Commodities Futures Trading Commission, and State Attorneys General.[12]

The informal consulting relationship between the antitrust enforcement agencies and the USDA was formalized last summer, when the FTC, DOJ and the USDA signed a Memorandum of Understanding Relative to Cooperation With Respect to Monitoring Competitive Conditions in the Agricultural Marketplace. This Memorandum is intended to ensure that the agencies will share information as appropriate and "confer regularly . . . consistent with applicable confidentiality restrictions, to discuss law enforcement and regulatory maters related to competitive conditions in the agricultural marketplace."

Agricultural investigations are already subject to multiple investigations by State Attorneys General. Although the DOJ and the FTC closely scrutinize all local competitive issues raised by a proposed merger, the State Attorneys General provide yet another level of local review. There is an established formalized protocol for the federal enforcement agencies and the State Attorneys General to coordinate concurrent merger investigations.[13]

In deciding whether to investigate a proposed transaction, the DOJ considers concentration levels in the affected industry. In industries with high concentration levels, there is a substantial likelihood that a proposed merger will be subject to a formal and extensive antitrust

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[12] Remarks by Douglas Ross, Special Counsel for Agriculture, Antitrust Division, DOJ, "Antitrust Enforcement and Agriculture," before the 2000 USDA Agricultural Outlook Forum, Arlington, VA (Feb. 24, 2000).

[13] *See* Protocol For Coordination in Merger Investigations Between the Federal Enforcement Agencies and the State Attorneys General (Mar. 11, 1998), reprinted at, 6 Trade Reg. Rep. (CCH) ¶ 13,420.

review.[14] These investigations are exhaustive. Consider that in the course of the DOJ's investigation of the Cargill/Continental Grain merger, the Department's investigative team, which consisted of approximately 20 lawyers, paralegals, and economists: reviewed over 400 boxes of documents, furnished by the parties pursuant to the DOJ's second request discovery procedures; deposed Cargill and Continental Grain executives; reviewed relevant legal and economic literature; consulted with officials of the USDA, the Commodities Futures Trading Commission, and State Attorneys General; and interviewed over 100 farmers, farm organizations officials, agricultural economists, grain company executives, and other individuals with knowledge of the industry and competitive conditions.[15] As detailed below, this exhaustive investigation led the DOJ to find that the anticompetitive effect of the proposed merger, absent divestitures and other remedies, would likely be lower prices paid to family farmers for their crops than they would otherwise receive absent the merger.

The Antitrust Principles Followed by the Antitrust Enforcement Agencies Fully Comprehend Competition Issues in the Agricultural Sector

The principal standard for merger enforcement is Section 7 of the Clayton Act, enacted in 1914, which prohibits the acquisition of stock or assets "where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly." [16] The focus of this standard

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[14] Statement of John M. Nannes, Deputy Assistant Attorney General, Antitrust Division, DOJ, Hearing on Competitiveness in Agriculture, House Judiciary Committee, at 5. (Oct. 20, 1999).

[15] U.S. v. Cargill and Continental Grain, No. 99-1875 (D.D.C. Feb. 11, 2000) (United States Response to Public Comments).

[16] 15 U.S.C. §18 (1988).

is to determine the competitive effects of a proposed merger in the future. The antitrust enforcement agencies jointly have developed the Horizontal Merger Guidelines to describe the inquiry they will follow in analyzing mergers.[17]

The Merger Guidelines recognize that market power encompasses the ability of a single buyer (a "monopsonist"), or multiple buyers ("oligopsonists"), to exercise market power and depress the price paid for a product to a level that is below the competitive price and thereby depress output.[18] The law further recognizes that such buyer power has adverse competitive effects comparable to those associated with the exercise of market power by sellers.[19]

Recent Enforcement Actions Involving Agribusiness Transactions.

The antitrust agencies' current approach to agribusiness merger review has resulted in more aggressive enforcement of our nation's antitrust laws than in any other sector of the economy. For instance, in all other sectors of the economy the DOJ defines markets using a five to ten percent price increase test. In the agricultural markets, it uses a one percent price increase test.

The DOJ's concerns with monopsony power figured prominently in its investigation and resulting consent decree in the Cargill/Continental Grain merger. As the Economics Director of Enforcement for the Antitrust Division of DOJ explained, in that case, the monopsony harm did not spill-over to consumers, or to national processors like Kellogg that sell final product to

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[17] U.S. Dept. of Justice & Federal Trade Comm., Horizontal Merger Guidelines (1992) (the "Merger Guidelines").

[18] Merger Guidelines, §0.1 (1992). *Cf. In re* Beef Indus. Antitrust Litig., 907 F.2d 510, 514-16 (5th Cir. 1990), United States v. Syufy Enters., 903 F.2d 659,663-71.

[19] *Id.*

consumers. Instead, the loss from the parties' increased monopsony power, absent the divestitures, may have been limited to grain suppliers, such as farmers and other grain sellers.[20] The DOJ concluded from its investigation that the lessening of competition resulting from the merger would likely have led to farmers receiving less money for their crops than they would absent the merger. In July 1999, the DOJ challenged the Cargill/Continental Grain merger as originally proposed and filed a complaint and proposed consent decree in court.[21]

To resolve the DOJ's competitive concerns, Cargill and Continental Grain were required to divest a number of grain facilities throughout the Midwest and in the West, as well as in the Texas Gulf. The DOJ insisted on divestitures in three different geographic markets where both Cargill and Continental operated competing port elevators, including Seattle, Stockton, California and Beaumont, Texas, three locations where their elevators competed to purchase grain and soybeans from farmers.

The DOJ also required divestitures of river elevators along the Mississippi River in Illinois and Missouri, and along the Illinois River, again where the merger would otherwise harmed competition for the purchase of grain and soybeans from farmers. An additional required divestiture was a port elevator in Chicago and a rail terminal in Troy, Ohio. Cargill is also prohibited from acquiring a rail terminal facility in Kansas that Continental had formerly operated and from acquiring a river elevator in Missouri, in order to protect competition for the

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[20] Remarks by Marius Schwartz, Economics Director of Enforcement, Antitrust Division, DOJ, "Buyer Power Concerns and the Aetna-Prudential Merger," presented at the 5th Annual Health Care Antitrust Forum, Northwestern University School of Law, at 5 (Oct. 20, 1999).

[21] U.S. v. Cargill and Continental Grain, No. 99-1875 (D.D.C. July 8, 1999) (Complaint and Proposed Final Judgment).

purchase of grain and soybeans. Finally, the DOJ required Cargill to enter into a "throughput agreement" to make a percentage of its loading capacity at a river elevator in Illinois available for leasing to an independent operator.

While not necessarily an exhaustive list, other agricultural transactions investigated by the DOJ include Monsanto's acquisition of DeKalb Genetics Corporation, a 1998 acquisition in the biogenetics area. Both companies were leaders in corn seed biotechnology and owned patents that gave them control over important technology. To satisfy the DOJ's concerns regarding how the merger would affect seed competition, Monsanto spun-off to the University of California Berkley its claims to a new technology used to make corn seed insect resistance.

In another proposed seed transaction, in 1999 Monsanto abandoned its proposed acquisition of Delta & Pine Land Co., which would have combined the country's two largest cotton seed companies, after learning of the DOJ's intention to sue to block the acquisition.[22]

In another enforcement action to protect farmers as buyers of farm machinery, in November of 1999, the DOJ filed a compliant challenging the Case/New Holland acquisition as originally announced. To resolve the Division's competitive concerns that the proposed transaction would result in higher prices for farm machinery, New Holland Co. agreed to sell its four-wheel-drive and large two-wheel-drive tractor businesses, and Case Corp. agreed to spin off its hay tool business.

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[22] Ross, supra note 12.

The Proposed Bills Would Impose Different Legal Standards From Those Employed by the Antitrust Enforcement Agencies for Almost a Century

The proposed legislation would impose legal standards for agribusiness merger review that are different from, and vague compared to, the well-defined antitrust standards applied by the antitrust enforcement agencies since the early 1900's. For example:

- S. 2552 authorizes the USDA to challenge an agribusiness acquisition or merger if the Department believes that the transaction would cause "substantial harm" to the ability of "independent producers and family farmers" to compete in the marketplace, while Section 7 of the Clayton Act requires the ultimate test of whether the proposed merger may tend substantially to lessen competition.
- The questions posed by S. 2552 include what constitutes "substantial harm," is it enough that one family farmers could be "substantially harmed" as a result of the proposed merger, and who is the family farmer? (S. 2552 does not define independent producers and family farmers.)
- Under S. 2552, the USDA would consider, among other factors, whether the proposed merger would "adversely affect producers in a particular regional area, including an area as small as a single State." This standard departs from merger analysis under Section 7 and the Merger Guidelines. To assess a potential adverse competitive effect, the antitrust enforcement agencies must define the relevant product and geographic market in which the parties to the proposed merger compete, and then determine whether the merger would lessen competition in those markets. Defining markets is a fact-intensive endeavor which requires the

agencies to ascertain whether, with respect to a product offered by the merging parties, there are alternative products to which customers could reasonably turn if the merging parties were the only suppliers of the products and sought to increase prices. The standard in S. 2552 does not require this critical competitive analysis.

- S. 2411 empowers the Secretary of Agriculture to declare unlawful a proposed agricultural merger that "could be significantly detrimental to the present or future viability of family farms or ranches or rural communities in the areas affected by the merger or acquisition, pursuant to standards established by the Secretary " or that "could" lead to "unfair practice" as defined in Section 4 of the bill. Again these are subjective and vague standards by which to challenge a proposed merger, and they are inconsistent with established antitrust law. For example, what constitutes "significantly detrimental" and to whom? ("Family farms, ranches and rural communities" are not defined.)
- Another example in S. 2411 of the vague standards that can be the basis for USDA to block a merger is the Section 4 "unfair practices" list. This list includes "to engage in or use any unfair, unreasonable, unjustly discriminatory, or deceptive practice or device in the marketing, receiving, purchasing, sale, or contracting for the production of any agricultural commodity." What, for example, is an "unreasonable" purchase of an agricultural commodity?

<u>There is No Evidence That Change is Needed</u>

The current approach to agribusiness merger review facilitates the strong presumption

favoring cohesive and harmonized U.S. competition policy and standards. Any departure from the current approach should require a showing that the current approach has failed. Such a showing requires proof that specific adverse competitive effects have resulted from FTC or DOJ approved mergers. I am not aware of any such evidence. Quite simply, the DOJ and the FTC have aggressively enforced the antitrust laws relating to consolidation in the agriculture sector.

Annex 1-B
International Competition Policy Advisory Committee
Biography of Members

Co-Chairs:

James F. Rill: Senior Partner with Collier, Shannon, Rill & Scott, PLLC. He has been practicing exclusively antitrust, competition, and merger law for almost 40 years. From 1989 to 1992, Mr. Rill was the Assistant Attorney General, Antitrust Division, U.S. Department of Justice. As AAG, he was responsible for negotiating the 1991 U.S.-EU antitrust cooperation agreement. Mr. Rill is a former Chair of the American Bar Association's Section of Antitrust Law, and is current Vice-Chair of the International Business and Industry Advisory Committee to the OECD Competition Law and Policy Committee. He is author and contributor to numerous publications and serves on the editorial board of BNA *Antitrust and Trade Regulation, The Antitrust Bulletin*, and the *Antitrust Report*.

Paula Stern: President of The Stern Group, Inc., an economic and trade analysis firm providing advice on international competitiveness policy and regulatory matters. As Commissioner and Chairwoman of the U.S. International Trade Commission from 1978 to 1987, the Honorable Dr. Stern analyzed and voted on over 1,000 trade cases across a spectrum of industries and agriculture. Dr. Stern serves on many public policy councils, including the President's Advisory Committee for Trade Policy and Negotiations. She is an author and public speaker on trade and foreign policy, Congress-Executive relations, women's issues, and U.S. relations in the Middle East, Asia, Europe and Latin America.

Executive Director:

Merit E. Janow: Professor in the Practice of International Trade at Columbia University's School of International and Public Affairs (SIPA). She is also Director of the International Economic Policy program at SIPA and Co-Director of Columbia's APEC Study Center. From 1990-93, she served as Deputy Assistant U.S. Trade Representative for Japan and China. At USTR, she was involved in the negotiation of over a dozen trade agreements. Previously, she practiced corporate law with Skadden, Arps, Slate, Meagher & Flom in New York. She is fluent in Japanese and is the author of several books and numerous articles.

Committee Members:

Zoë Baird: President of The Markle Foundation. Formerly Senior Vice President and General Counsel at Aetna, Inc. Ms. Baird has worked for General Electric as Counselor and Staff Executive and was a partner in the law firm of O'Melveny & Myers. She is a member of the Council on Foreign Relations, the American Law Institute and the James A. Baker III Institute for Public Policy. Ms. Baird serves on the Board of the Brookings Institution and the President's Foreign Intelligence Advisory Board.

Thomas E. Donilon: Senior Vice President, General Counsel and Corporate Secretary, Fannie Mae. Formerly a partner with the firm of O'Melveny & Myers. From 1993 to 1997, Mr. Donilon served as Assistant Secretary of State for Public Affairs and as Chief of Staff to Secretary of State Warren Christopher, for which he received the State Department's highest award, the Secretary of State's Distinguished Service Award. Mr. Donilon is currently co-chair of the Council on Foreign Relations' Congress and United States Foreign Policy Program.

John T. Dunlop: Lamont University Professor, Emeritus at Harvard University. He is a past Chairman of the Department of Economics at Harvard, former Dean of the Faculty of Arts and Sciences, and was acting Director of the Business and Government Center at the School of Government. Secretary of Labor during the Ford Administration. Professor Dunlop is the author of numerous books on wages and industrial relations. He is a Life Member of the National Academy of Arbitrators.

Eleanor M. Fox: Walter J. Derenberg Professor of Trade Regulation at New York University School of Law. She was a partner and is counsel at Simpson Thacher & Bartlett. She has served as Commissioner on President Carter's National Commission for the Review of Antitrust Laws and Procedures, as Chair of the Antitrust Law Section of the New York State Bar Association, as Vice President of the Association of the Bar of the City of New York, and as Vice Chair of the ABA Antitrust Law Section.

Raymond V. Gilmartin: Chairman of the Board, President and Chief Executive Officer of Merck & Company, Inc. Mr. Gilmartin is former Director and Chairman of the Pharmaceutical Research and Manufacturers of America and Chairman of the Healthcare Leadership Council. He is also a Director of the College Fund/The United Negro College Fund and a member of the Business Roundtable, the Business Council, and the Council on Competitiveness.

Vernon E. Jordan, Jr.: Senior Managing Director, Lazard Frères & Co. LLC; Of Counsel, Akin, Gump, Strauss, Hauer & Feld. Mr. Jordan was President of the National Urban League, Executive Director of the United Negro College Fund, and Attorney-Consultant to the U.S. Office of Economic Opportunity. He also has served on the President's Advisory Committee to the Points of Light Initiative Foundation, the Secretary of State's Advisory Committee on South Africa, and the Advisory Council on Social Security. Mr. Jordan is a member of the American Law Institute, the National Bar Association and the Council on Foreign Relations.

Steven Rattner: Deputy Chairman of Lazard Frères & Co. LLC. Mr. Rattner founded Lazard's Communications Group. Before beginning his investment banking career in 1982 with Lehman Brothers Kuhn Loeb Incorporated, Mr. Rattner was employed by The New York Times as a correspondent in New York, Washington and London, specializing in economic and energy matters. Mr. Rattner is Chairman of the Educational Broadcasting Corporation, a Trustee of the Brookings Institution and a member of the Council on Foreign Relations. In 1994 Mr. Rattner was named a Global Leader for Tomorrow by the World Economic Forum.

Richard P. Simmons: Chairman of the Board of Allegheny Technologies Incorporated. In addition to his role as Chairman of Allegheny Technologies, he is a member of the Executive Committee of Allegheny Conference on Community Development. He is also a life member of

the MIT Corporation and a director of PNC Bank Corporation. Mr. Simmons is a director and past Chairman of the United Way.

G. Richard Thoman: President and Chief Executive Officer of the Xerox Corporation. Prior to joining Xerox, Mr. Thoman was Senior Vice President and Chief Financial Officer of the IBM Corporation. He is a member of the Council on Foreign Relations, The Business Council, and The Business Roundtable. He is also a director of DaimlerChrysler, a trustee of the Museum of Modern Art, a board member of the Americas Society, an advisory board member of the Yale University School of Business and the Fletcher School of Law and Diplomacy.

David B. Yoffie: Max and Doris Starr Professor of International Business Administration, Harvard Business School. Chairman of the Competition and Strategy Department and Chairman of the Advanced Management Program, Professor Yoffie also ran the School's international executive program, Managing Global Opportunities, and directed Harvard's four year research project on international trade. He is a widely published author on international business, technology, and competitive strategy.

Counsel:

Cynthia R. Lewis: Before joining the Advisory Committee as counsel, Cynthia Lewis was an associate with the law firm Skadden, Arps, Slate, Meagher & Flom from 1993-1998. While at Skadden she practiced with the Antitrust and EC Law departments in New York and Brussels, Belgium where she analyzed mergers under U.S. and European competition laws. She also assessed antitrust filing requirements in the U.S., Europe and the rest of the world on behalf of clients engaged in multinational transactions. She graduated *magna cum laude* from Georgetown University Law Center in 1993.

Andrew J. Shapiro: Before joining the Advisory Committee as counsel, Andrew Shapiro was an associate with the Washington law firm of Covington & Burling from 1995-1998 practicing with the international, litigation, and antitrust practice groups. He graduated from Columbia University School of Law in 1994 as a Harlan Fiske Stone Scholar and received a Master's Degree in International Affairs from Columbia University's School of International and Public Affairs in 1995. He is a term member of the Council on Foreign Relations.

Stephanie G. Victor: Ms. Victor joined the Advisory Committee as counsel with a background in international litigation and interagency enforcement cooperation after spending several years with the U.S. Commodity Futures Trading Commission. Previously, she practiced antitrust and trade law as an associate with the Washington law firm of Ablondi, Foster, Sobin and Davidow. Ms. Victor is a 1990 graduate of the Georgetown University Law Center and earned her undergraduate degree from the University of Pennsylvania in 1985. She is fluent in French.

Testimony before the Senate Agriculture Committee

April 27, 2000

David C. Nelson

What's going on in agribusiness? The financial performance of agribusiness companies and agribusiness stocks has been poor. Since January 1997, my Agribusiness Stock Index is down by one-third, during one of the greatest bull market runs in history – a time over which the S&P 500 has doubled . This is due to negligible returns on capital, slow and volatile earnings growth, and an implied unattractive outlook for future returns in this sector.

Poor stock price performance reflects weak earnings growth across the sector in the past, but what stock prices reflect are the market's forecast for future profitability. It is clear from the voting booth of the stock market, that investors are voting with their feet to dis-invest in agribusiness

Why have returns been so poor? A few thoughts:

The value chain across the entire food industry is contracting. There is a power shift taking place from food companies to retailers, but also from retailers to consumers. The profit challenge being faced by farmers is not unique across the food chain.

Customer and consumer needs and preferences change, and are changing at an increasing rate. Corn movement, for instance, has shifted from being based largely on exports to being more focused on the domestic processing industry. With this shift, substantial assets and investments have become out of place and of little to no value. Shift happens in our economy of creative destruction.

Commoditization. Companies need to generate differentiated new products to maintain consumer interest and pricing power. Innovations are rapidly duplicated and the ability to capture value, even when successful, is often short lived.

New competition. As an example, soybean processors are getting new competition from Brazil and China – as well as from domestic cooperatives. These players have different economics and different return objectives that make competition difficult for profit oriented companies with public shareholders.

Essentially, we have too many companies fighting for too few profits. Agribusiness will not attract the capital it needs to make the investments farmers say they want until profitability improves.

Why do we see consolidation and integration? Industry consolidation and integration occur for two main reasons.

One, companies and individuals often need to sell their business because they are unprofitable or unviable in their current structure or configuration. This can happen for many reasons, perhaps the most frequent of which is that businesses fail to change appropriately with a changing environment. In agribusiness, these are primarily family owned operations, frequently within a generation of leaving the farm.

This is a natural selection process at work. This is the reason we have the most productive and efficient food system in the world. This is the reason we have a healthy economy and a reason why other economies with more intrusive policies have high unemployment and dis-investment.

Two, we are seeing integration occur to meet the demands of customers and consumers. We are hearing a lot of objections, for instance, to packer ownership of livestock these days, particularly in the pork sector. This is not because raising hogs is sexy or glamorous and something packers want to do. It is because they have to. Customers (retailers and restaurants) and consumers want quality and consistency. You cannot

have quality and consistency without coordination or integration. As an analyst, I would rather see companies investing forward in the production chain to add value through further processing or branding. These companies are investing backwards in the chain not because they want to, but because they have to serve the consumers' demands for quality and consistency.

It is important to note that not only are customers of food manufacturers more demanding, but they too are consolidating. The top five supermarket chains have gone from roughly 25% market share in 1995 to 40% share today. These chains want and need suppliers with regional and national distribution. Supermarkets are trying to simplify operations by reducing the number of suppliers, like all businesses. They also need suppliers that have made the substantially and continually increasing investments in information technology necessary to extract supply chain cost savings. Food industry consolidation has been much less than at the retail level, and what has taken place is partially in response to what is taking place among their retailer customers.

A Wall Street perspective on proposed legislation to impose higher standards on agribusiness mergers and acquisitions. Our review of certain proposed legislation that would impose additional USDA oversight and approval regarding agribusiness mergers and acquisitions, leads us to believe such legislation would negatively impact investment in agribusiness and agriculture. Under such a scenario, these companies' ability to defend themselves in a rapidly changing economy could become compromised. This risk creates uncertainty that would reduce the value of existing assets. The ability of agribusiness companies' to generate a return on capital and attract important new capital would be negatively impacted.

These are capital intensive industries that require substantial reinvestment merely to stay in the game. For instance, IBP has announced plans to double its capital expenditures over the next year to near $400 million, in large part to fund new equipment and technology for case-ready meat to make their beef and pork products more competitive with chicken. In addition, the meat industry has invested at least $300 million in the last three years to fund food safety initiatives, in particular related to new HACCP requirements. Expenditures necessary to meet environmental standards are also rising rapidly. Packers need to be sufficiently profitable to meet competitive, food safety and environmental standards, or we will continue to see dis-investment in this industry and producers will simply have fewer places to sell their livestock.

This high degree of capital intensity is an unattractive feature to investors. This is why meat packers such as IBP and Smithfield trade at price to earnings ratios near 5x, while the overall market is at 27x. This obviously reflects that capital is much more expensive for packers than for industry as a whole.

Policy considerations.

1. Make a conscious decision on the nature and direction of agricultural policy. In my opinion, we need to make a conscious decision regarding what sort of farm policy we want in this country. We passed the Freedom to Farm Act in 1996 but since then we have also seen bailout packages every year. Those that provide the money to finance this industry would prefer predictability in policy, rather than these one-off packages we've had in recent years.

2. Level the playing field on trade policy. Agricultural trade and production continue to be highly distorted by the large production and export subsidies of the European Union. U.S. farmers and U.S. based agribusiness is inherently handicapped by this distortion.

3. Help farmers adapt to the changing economy, rather than further entrench them in nonviable operations. Our economy is based on creative destruction. Farmers and other businesses need to adapt to changes in our economy, or find other ways to make a living. Most non-farmers now have many different jobs throughout their careers and often have to move their families around just to keep up with changes in the economy. Change isn't easy, or even pleasant. But maybe agricultural policy should be more focused on helping farm and rural families to adapt to the new economy rather than trying to preserve them in operations that simply aren't viable.

Competition, Concentration and Agriculture

Statement to the Senate Committee on Agriculture, Nutrition, and Forestry
Agriculture Concentration and Competition Hearing
April 27, 2000

Professor Peter C. Carstensen
Young-Bascom Professor of Law
University of Wisconsin

For more than 25 years I have been a teacher and scholar of economic regulation and competition policy. In particular, my work has focused on the theory, policy and actual enforcement of our antitrust law. Prior to going to teach at the University of Wisconsin, I was a staff attorney at the United States Department of Justice Antitrust Division. There I was assigned to the Evaluation Section where my projects included a wide range of competition policy issues. I hold both an LLB degree and a Masters in Economics from Yale University and have consistently sought to relate economic analysis to the public policy problems that arise in the effort to foster and retain competitive markets. I am also a generalist with respect to the areas of economic activity that I examine.

Over the years, however, I have had a number of opportunities to examine specific agriculturally related topics. For example, as a government lawyer I conducted an examination of the old meat packers consent decree from1920 and recommended modernization of its terms to take account of the fact that the industry had, by the late 1960s, become much more competitive. Regrettably, it took some years before those recommendations were ultimately implemented and then the government gave up too much control over the structure of the industry. In 1992, I published a detailed study based on primary sources of the famous *Chicago Board of Trade* case (Board of Trade of the City of Chicago v. United States, 246 US 231 (1918)) which concerned

price fixing restraints in grain trading and remains the primary doctrinal statement of the rule of reason in antitrust law.[1]

A little over a year ago I became more actively engaged in the problems of competition in agriculture as a result of inquiries about competition policy issues from both congressional staff members and farm organizations. Since then, I have had the opportunity to participate in meetings and conferences that address various aspects of agriculture. I am still not an expert in the details of the operation of agriculture and its economics, but what I am learning is that the fundamental issues concerning competition and concentration in agriculture are similar to issues in any other area of business activity.

The Sherman and Clayton Acts were adopted because Congress was concerned with the social and political as well as the economic implications of high concentration, monopoly, conspiracy, and massive mergers. In proposing the act that bears his name, Senator Sherman (R., Ohio) warned the Senate that: "The popular mind is agitated with problems that may disturb social order, among them all none is more threatening than the inequality of condition . . . and opportunity that has grown . . . out of the concentration of capital into vast combinations to control production and trade and to break down competition." Later in the same great speech, he observed: "If we will not endure a king as a political power we should not endure a king over the production, transportation, and sale of any of the necessaries of life. If we would not submit to an emperor we should not submit to an autocrat of trade, with power to prevent competition and to

[1] Peter C. Carstensen, The Contents of the Hollow Core of Antitrust: The *Chicago Board of Trade* Case and the Meaning of the "Rule of Reason: in Restraint of Trade Analysis, 15 **Res. in Law and Econ**. 1 (1992)

fix the price of any commodity."[2] These declarations demonstrate that core political values were central to the concerns that motivated the adoption of antitrust law.

In the first substantive decision interpreting the Sherman Act, Justice Peckham, no liberal or protectionist, wrote that the dynamics of markets can bring unavoidable hardships to particular classes of business. Such transformations are inevitable and must be endured. However, he condemned "combinations of capital whose purpose . . . is to control . . . production or manufacture . . . and . . . dictate price. . . ." In addition to the harm to consumers, he identified the harmful effect of "driv[ing] out of business . . .independent dealers . . ." He concluded: "[I]t is not for the real prosperity of any country that such changes should occur which result in transferring an independent business man . . . into a mere servant or agent of a corporation. . . ; having no voice in shaping the business policy . . . and bound to obey orders issued by others."[3]

Other seminal decisions of the courts have carried forward this theme. For example, Judge Learned Hand in the *Alcoa* case declared: "[I]t is possible, because of its indirect social or moral effect, to prefer a system of small producers . . . to one in which the great mass of those engaged must accept the direction of a few."[4] Similarly, Justice Marshall in *Topco* declared that: "Antitrust laws in general, and the Sherman Act in particular, are the Magna Carta of Free enterprise. They are as important to the preservation of economic freedom and our free-enterprise system as the Bill of Rights is to the protection of our fundamental personal

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[2] Quoted in Hans Theorelli, **The Federal Antitrust Policy,** 180 (1955)

[3] U. S. v. Trans-Missouri Freight Ass'n., 166 U.S. 290, 323-324 (1897).

[4] U. S. v. Aluminum Co. of America, 148 F.2d 416, 428 (2nd Cir. 1945).

freedoms."[5]

I want to renew these warnings in the context of what is happening to agricultural markets today. Past failure to enforce antitrust law has resulted in increased concentration in both the markets supplying agriculture and in those that process and distribute its products. Moreover, subsequent, large scale vertical integration through both ownership and contract has impaired the working of transactional markets in agricultural goods. More and more, we see a handful of firms dominating a larger number of markets on both sides of the farmer and rancher. Further, those firms in turn are entering into "strategic alliances" with each other to make more secure their joint control over and allocation of markets. These changes encourage, indeed, may make inevitable, conduct that further weakens not only the viability of existing agricultural producers but also has a strongly negative impact on the dynamics of our economy as a whole. Fearing the strategic behavior of its rivals, each agricultural behemoth responds with actions that it believes will protect its position even though this imposes costs on producers and consumers. These 800 pound gorillas trash the agricultural economy to protect and entrench their present and future position in the market. The farmer and rancher increasingly has "no voice in shaping the business policy" but is simply "bound to obey orders issued by others." Once independent farmers and ranchers are becoming the serfs of the 21st century.

Even if one were to ignore the social and political reasons for favoring a dispersed and open form of economic organization for our society, powerful economic considerations support the same policy goal. The fundamental reason for our economic success in this country is not short run efficiency in production, but the continued capacity to innovate new products, services,

[5] U.S. v. Topco Associates, Inc., 405 US 596, 610 (1972)

methods of production, and systems of distribution. It is essential to our long-run economic growth that we retain the kind of open economy in which such dynamic growth can occur. Such essential innovation and adaption can and will occur with greater speed and more general social gain when markets are unconcentrated. Competition is a great force leading to innovation as well as adoption of more efficient and desirable methods of production and distribution. Moreover, in open and competitive markets, the incentives to engage in strategic behaviors whether to exclude rivals or exploit unreasonably customers or suppliers are greatly limited because of the capacity of others to enter and compete.

Thus, competition policy should not make short run economic efficiency a central criterion. Experience teaches that there are many ways to achieve such efficiency. Hence, policy makers and competition law enforcers should seek those ways of organizing economic activity and market relationships in order to maximize the potential to achieve other essential goals of public policy. For social and political reasons as well as a long interest in the maintaining the dynamics of the economy, large concentrations of control over specific markets or market sectors are undesirable. Moreover, it is very rare in an economy as vast as ours that high concentration is necessary to achieve desirable efficiency.

I am not suggesting that we should ignore the questions of economic efficiency and minimizing the costs of production. Those are always threshold considerations. They provide a powerful argument against many of the protectionist pieces of legislation proposed in state and national legislatures. My claim supported by many decades of experience is that the market process can find ways to achieve real efficiency without having to sacrifice other important goals.

One of our most important goals for reasons of economic dynamics and social and

political values is to retain and enhance a truly competitive market structure. There are those, some of whom may be present here today, who, in the spirit of Karl Marx, will tell you that there is only one way to organize an economy and that is to centralize it and have one or at most a handful of enterprises. The fall of the Soviet system should have taught everyone that economic determinism and the cult of giantism are invalid. As Mao said in a different context there are "many roads" whether to socialism or capitalism. We need to choose the road that is most consistent with our social, political and long run economic needs and aspirations.

The fact that there are many roads to efficiency is liberating for public policy. It means that decision makers need be much less concerned about long run adverse efficiency effects of their decisions. If something is truly efficient, the market will find a way to achieve that outcome. A decade ago I reviewed a number of the claims by scholars about the adverse effect of antitrust actions on the economy.[6] These cases were largely ones that had emphasized non-efficiency values. The historical record simply did not support the claim that those decisions had caused serious losses or other negative effects. Regrettably, I should also report that it is a little difficult to find strong evidence that antitrust interventions standing alone had had clearly positive effects on efficiency. More often than not, it was the interaction of antitrust, which had retained a more open and accessible market context, with changes in technology and/or other regulation that produced significant improvements.

The data I have seen show that the country faces very high and rapidly increasing levels of concentration in both industries supplying farms and in those buying farm products. In general,

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[6]Peter C. Carstensen, How to Assess the Impact of Antitrust on the American Economy: Examining History or Theorizing, 74 **Iowa L. Rev**. 1175 (1989).

high concentration results in higher prices to buyers and lower prices to sellers than would occur in less concentrated contexts. This seems to be the situation facing agriculture.

In addition, high concentration makes it rational and feasible for firms to engage in a variety of strategic actions including longer term contracts for supplies, exclusive dealing, slotting allowances, and other conduct which make sense because of the impact on competitors–actual or potential–rather than on the underlying costs of doing business. These practices often result in lower prices to producers. Some mistakenly believe that such a use of market power will aid the ultimate consumer by lowering prices.

The notion that a monopoly buyer will share its winnings with its customers is wrong. Recently, Frederick Warren-Boulton, who directed economic operations at the Antitrust Division in the Reagan years, reiterated the basic economic analysis that firms with such buying power can exploit that power to the detriment of sellers and that, regardless of the degree of competition in the downstream markets into which such firms sell, they have no incentive to "pass-on" to consumers any of the excess profits derived from exploiting suppliers.[7] Indeed, if the downstream market is also oligopolistic, such a firm will simultaneously over charge its customers.

Nevertheless, in the 1980s the government failed to police the mergers among meat packers. It mistakenly assumed that downstream markets would somehow police the upstream strategic buying conduct of regionally dominant firms. The antitrust enforcement authorities ignored the lost choices that these combinations imposed on farmers and ranchers. Today, we have highly concentrated markets on both a national and regional basis. As of 1998 four firms

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[7] Frederick Warren-Boulton, The Case Against An "Agrarian Antitrust Policy." A paper presented at the Agricultural Outlook Forum 2000, February 24, 2000.

slaughtered 81% of all steer and heifers.[8] This is an increase from 36% of total slaughter in 1980. Similarly, hog slaughter rose from 34% in the top four firms in 1980 to 56% in 1998.[9] The result is strategic buying behavior which harms farmers and ranchers, denies them a transparent transactional market place for their products, and may now require more direct regulation of buying practices. Recent data show that the spread between the price paid to raisers and the wholesale price of meat has increased substantially. According to USDA data, the farm-to-wholesale price spreads for pork increased by 52% and for beef by 24% in the past five years.[10] This is exactly the result that theory would predict as oligopoly grows in both the buying and selling markets for meat products.

Other markets into which farmers and ranchers sell have also become more concentrated. This is notable in grain processing[11] and is an increasing source of concern in dairy products as well. I have seen published reports that one company has acquired control over 70% of all milk sales in New England and has a 20% share of all sales in the United States as a result of an aggressive merger program.

Further undermining the vitality of the market system was the tolerance of mergers among grocery retailers which allowed greater and greater concentration of buying power in the hands of

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[8] James Baker, Administer of Grain Inspection, Packers and Stockyards Administration, in testimony before the Senate Agriculture, Nutrition and Forestry Committee, Feb. 1, 2000.

[9] Id.

[10] Robert Taylor, The Closing Circle of Global Food Companies. A paper presented at a Democratic Policy Committee hearing, April 5, 2000.

[11] For example, there is high concentration in flour milling, wet corn milling, soybean milling, cottonseed milling and malting. James M. MacDonald, Concentration in Agribusiness, Table 2. A paper presented at the Agricultural Outlook Forum 2000, Feb. 24, 2000.

large enterprises. This created a symbiotic vertical relationship between retail oligopoly and the slaughter house oligopoly. The result is the increasing spread between the price paid the farmer the price charged the housewife.

Over the last two decades there has also been a marked increase in the concentration of the various industries serving agriculture–from farm equipment to seeds and herbicides or pesticides.[12] Among leading foreign and domestic seed companies alone, there have been 68 acquisitions between 1995 and 1998.[13]

The late Leonard Weiss in 1989 collected all the studies he could find concerning the comparative impact of concentration on price.[14] The overwhelmingly consistent outcome was that prices were higher in concentrated markets even though profits were not consistently higher. The implication of these results is that concentrated markets impose costs on consumers and suppliers who must sell into such markets, but such markets are not more efficient. The oligopolists waste enormous resources in striving to retain, protect and entrench their market positions.[15] Thus, there is no social gain. There is only social cost.

The beef packing industry illustrates how unnecessary high concentration is to efficient plant scale. As of 1997, the four largest firms control 78% of the slaughter. But there were 22

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[12] For example, MacDonald, supra, in Table 4 shows that high levels of concentration exist in production of seeds for wheat, corn, soybeans, and cotton.

[13] Id.

[14] Leonard Weiss, ed., Concentration and Price (1989); see also Peter C. Carstensen, While Antitrust Was Out to Lunch: Lessons from the 1980s for the Next Century of Enforcement, 48 **SMU L. Rev.** 1881 (1995).

[15] See, Richard Posner, The Social Costs of Monopoly and Regulation, 83 **J. Pol. Econ.** 807 (1975).

plants with the highest level of production accounting for 80% of all production. Assuming that such plants reflected the greatest scale economies in operations, achieving such scale economies would require less than 3.7% of the market. In pork, the 31 largest plants yield 88% of production which means each plant requires less than 3% of the market.[16] Thus a highly dispersed ownership and unconcentrated market would be entirely consistent with the largest size of plants in both pork and beef packing.

In framing and enforcing a policy to retain and enhance individual autonomy and freedom of action, it is also important to recognize the broader implications of context. If large firms dominate a market sector, then it is irresponsible to look only at the specific points of substantial competitive interaction without considering how to maintain effective overall competition in that sector.

Illustrative of this error is the pending settlement of the Cargil-Continental Grain merger.[17] This merger combines two of a handful of global grain trading firms. The government insisted only on isolated divestitures where it identified specific quantitatively substantial overlaps between the merging firms. In many instances including key export facilities, not surprisingly, the prospective buyer of those assets is another of the few major global grain traders. Thus, global market leaders are cannibalizing a third firm. The Antitrust Division in its justification for the settlement recognized the pervasive competition between Cargil and Continental, but its proposed relief ignored the overall operation of grain trading in which large integrated firms have come to dominate. By allowing the dismemberment of one of the leaders, the government has effectively

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[16] MacDonald, supra, at Table 1.

[17] *U.S. v. Cargill, Inc.,* Civil No. 99-1875, DCDC, filed July 8, 1999.

reduced the number of real competitors in a significant way. This is a failure to consider the overall context because of blinders of a theory of competitive effect that ignores the larger and longer run implications of these combinations. This settlement will increase the risk of monopsonistic buying practices of the sort that Mr. Warren-Boulton described.

At the same time, there is no reason to believe that any increased efficiency will result from this merger. The Antitrust Division position is only that it did not see a significant present danger to narrowly defined competitive concerns arising from the combination less its divestitures. This is a bad decision because it reinforces the aggregate concentration of the market and thus entrenches the kind of oligopoly that will have resources to protect itself against equally efficient, socially more desirable alternatives. Moreover, by reducing in the long run the choices available to sellers, it will further limit the potential for autonomy and choice.

Review of the identify of buyers of agricultural products or sellers to agriculture producers shows that the same companies appear again and again. Thus DuPont provides insecticides and herbicides as well as providing Pioneer Hybrids.[18] Monsanto is also a leading producer of seeds and crop protections. On the other side, Cargil, ADM, or ConAgra appear again and again among the leading firms in various kinds of food processing and distribution.[19] Several implications follow from this kind of sector dominance as well as cross linkages among supply and processing markets. The first is that such firms have the potential to deal in multiple ways with their customers. Monsanto has employed contracts to limit the use of herbicides on the soy beans

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[18] MacDonald, supra, Table 4, lists DuPont, Monsanto, Novartis and Dow as the leaders in corn, soybean and wheat seed sales. Monsanto alone is the dominant firm in cotton seed.

[19] Id.

it sells to its particular brand. Thus, such a firm has an incentive to distort and restrict competition in order to further its owns economic interest.

A second important implication is that the potential exists for linked oligopoly. Firms recognize each others' "sphere of influence" and refuse to enter or compete vigorously in each others' dominant area. This has proven to be a noticeable consequence of interstate bank mergers.[20] It seems increasingly likely in the area of agriculture.

Third, limiting the number of firms in any sector reduces the incentive to engage in dramatic innovations in technology or marketing. The firms have a shared interest in stability within their sector. They can define and limit the scope of their competition with less risk that someone will come up with a new way to do things. This kind of concentration therefore chokes off the scope of innovation and competition among potential alternatives.

Increasingly producers have integrated backward into the production of agricultural commodities. The pending merger between Smithfield and Murphy Farms that will consolidate the largest pork processor with the dominant pig raiser illustrates the kind of combinations that are occurring across a large number of fields. Such integration will not produce efficiency gains. It will raise barriers to entry into both processing and raising hogs. As such integration increases, the transactional market will be marginalized. Independents will face greater obstacles in marketing their hogs and lower prices. The spot market will become the place in which the packer seeks only the extra supplies when there is unexpected demand. This is likely to result in a higher cost on average for the processor, but the gain will be in controlling more fully the market

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[20]Gary W. Whalen, Nonlocal Concentration, Multimarket Linkages, and Interstate Banking, 41 **Antitrust Bulletin** 365 (1996).

context–less risk of new entry, less risk of direct competition for supplies and thus more apparent predictability for the market process. On the retail end, the large chain buyer is as interested in being assured that its price is as favorable as its competitors price. Thus, the inefficiency of the system can be passed on to the final consumer.

The combination of these structural changes in turn make possible new kinds of conduct that are rational self-protection by such firms. These actions achieve both protection and entrenchment of their positions in the market. They produce no gains for consumers or farmers and ranchers. Indeed, this conduct is likely to harm the long run best interests of both classes. Several types of conduct problems seem evident:

> *Strategic alliances*: Non-merger collaborations among large firms allow them to coordinate their competition in order to create mutual power. The intended effect is to obtain a stronger market position. A few of these alliances might provide economically useful coordination if they create an efficiency enhancing joint venture to produce or distribute new products. Such joint ventures also show that merger is not an essential element to effective entry into new lines of business. Other alliances, to the extent that we have any reliable information, are merely a mechanism to coordinate efforts among firms to limit their direct competition and ensure mutual strategies to build market power.
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> It should be a source of real concern that we know so little about the scope and content of these alliances. The parties, except as required by law, do not make public disclosure of their agreements or how they are implementing them. Given the high levels of concentration both within markets and industry sectors as well as the growing vertical integration in these industries, such disclosure is essential to proper evaluation of these relationships.
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> *Vertical contracts*: The growth of contracts between processors and producers in a variety of agricultural commodities has produced an additional set of harms. These contracts have arguable utility by providing the producer with greater assurance of sale at a known price and by assuring the buyer that particular products will be available when desired. However, these contracts often have substantial non-efficiency motivation as I have discussed. In particular, if a producer can tie up a substantial segment of the existing supply under contract, it will be much more difficult for a new entrant to open up in the area because of the limited supply available. If a substantial segment of supply is controlled, it will destroy a workable transactional market; thus forcing the remaining

producers to scramble to seek similar contracts. In the end, such rivalry can destroy the more efficient and flexible means of linking producers to processors. The choices are not efficiency driven but the consequence of the rivalry that occurs in concentrated markets. One of the most difficult problems facing commercial agriculture today is that of gathering and interpreting pricing and other contract information.

Contracting is not inherently evil, but it can be used for a variety of strategic purposes if it does not take place in a well structured legal environment in which there is reasonable equality of bargaining power, limited incentive to engage in strategic behavior, and continuing transparency with respect to transactions. None of these elements are currently present in most agricultural dealings. I would note, however, that in Wisconsin, the state department of agriculture has adopted administrative rules governing the contracting for vegetables for processing. Those rules were the result of a series of sessions involving producers and processors as well as some individuals like myself. The result is a set of rules that govern the contracting process in ways that increase the fairness and equity of the resulting contracts for both parties.

Slotting and other special deals at retail: Recent congressional hearings have focused on the emergence of slotting payments as yet another device that creates problems throughout the agricultural marketing system. Large food processors pay large retail chains for the privilege of having their products displayed favorably. Such transactions occur because there are large producers with multiple lines of goods dealing with very large retail chains. Buying a favorable location in a single store for a single product of small firm does not produce either foreclosure or likely gain. In such a situation, the store owner will decide based on his or her own judgment what to place on the shelf and the producer will compete on price and quality. When a large producer can deal with a handful of chains so that it gets a favored position, this enriches the chain and protects the large producer from the threat of competition that arises from consumer choice. Again, this problem exists because of the concentrated markets in retailing and production.

Abuse of intellectual property rights: Increasingly, suppliers of seeds and other inputs to agriculture are trying to control the production and resale of the resulting crops and animals along with specifying the methods and products to be used in connection with raising these items. Here the problem is an expansive definition of the legal rights that patents and other intellectual property confer on their "owners." When a soy bean developer wants to control the herbicide or pesticide used with the beans its customer plants, we see the kind of distortion that such rights create. We have new technology in plants and animals protected by legal systems developed in another time to define rights in different contexts. These rights confer vast opportunities to exploit the user. This is true across the board in areas of high technology. By licensing rather than selling the idea, the owner can exercise comprehensive control over the scope and nature of the use made. In the concentrated markets of agriculture with the broad range of activities controlled by a single firm, these rights encourage a expansive and abusive exploitation of the user.

> Indeed, once one firm starts down this path, its rivals are forced to follow because otherwise, they risk losing out in the race to survive. Thus, badly defined rights and concentrated markets induce the maximum in exploitation.

In sum, the present structure and conduct of the markets supplying agriculture and buying its products impose substantial but avoidable costs on farmers and ranchers as well as consumers. Moreover, the gain in terms of innovation or efficiency are not uniquely associated with the present system. Indeed, it seems likely that the country would gain on both counts from a different system that reduced concentration and opened up alternative routes. Finally, the cost of this transformation is not only economic. It makes the farmer or rancher, in the words of Justice Peckham, "into a mere servant or agent of a corporation."

I should note that some marginal progress is occurring. The FTC has recently blocked Ahold's acquisition of Pathmark thus retaining some better competition in the grocery business. The FTC also insisted that the divestiture of gas stations by Exxon and Mobil in the northeast go to a single buyer so that the resulting entity would have a greater potential to be an effective competitive force. The Antitrust Division blocked Monsanto's effort to acquire dominance in the cotton seed business. In the Continental Grain merger, it did at least acknowledge that adverse effects on suppliers are legitimate antitrust concerns in addition to adverse effect on consumers. Moreover, the Division has in some high technology and telecommunications mergers recognized that both vertical and conglomerate dimensions of the transactions raised competitive concerns and required remedy. Much more would need to be done before the current enforcement of antitrust law could be regarded as a primary means to protect the existing structure of American agriculture from unnecessary disruption and potential destruction.

Three elements are important to a revived competition policy in light of the present structure and conduct of agriculturally related businesses. First, stricter enforcement of current merger law to challenge those acquisitions that increase market as well as sector concentration, weaken potential competition, or create excessive vertical integration. Such a policy should also seek more frequently to block transactions in their entirety rather than permit them subject to partial divestiture. Second, antitrust law should be used to revisit and challenge, when relief is still practical, those combinations which have most dramatically increased concentration. There is no statute of limitations on the Clayton Act's prohibition against anticompetitive mergers, but it will be difficult to induce either federal law enforcement agency to re-open old cases. The best hope is for attorneys general of affected states to pursue such cases jointly. Third, the reality appears to be that the context for both purchases by farmers and their sales of products has changed. Contracts of various lengths involving a number of risks and restraints are increasingly common. It is vital to create a legal framework in which these transactions occur that will provide better information to and fairer terms for farmers. Such rules necessarily should include prohibitions on per se unfair terms. The law provides greater or lesser protection for other small businesses dealing in franchise and dealership arrangements. If farmers and ranchers must enter into such transactions, they too are entitled to protection.

The first recommendation requires no substantial elaboration. Too often in the past and even today, those charged with enforcing the anti-merger provisions of the Clayton Act either fail to challenge transactions or settle for very modest and ineffective relief. The myth of merger as an efficiency enhancing necessity seems to be as pervasive as it is wrong. By taking a very narrow view of markets and limited recognition of adverse impacts, antitrust enforcers excuse their

inaction.

While the first best choice would be for the agencies themselves to be more assertive in enforcing the law, it is also appropriate to include additional participants in the process of reviewing such transactions. Several pending legislative proposals would give the Secretary of Agriculture a seat at the table when decisions to sue and to settle are being made. The Secretary's mission would be to guard the long term interests of agricultural producers. By bringing the expertise of the agency to bear on the questions of the likely harms of mergers and the potential adverse effects of specific settlements, the decision process can be improved. Currently, in electricity, telecommunications and banking, relevant federal agencies are involved in the decision process both by making their own decisions and by participating with the antitrust agencies in evaluating such transactions. Given the past failures of enforcement, it is time to include agriculturally related combinations in this category.

The second recommendation is beyond the scope of this committee or the legislative process. Because there is no statute of limitations on an anticompetitive merger, it is my emphatic suggestion that either the federal agencies or, more likely, the states should revisit and challenge those undesirable mergers for which remedy is still feasible. In the long run, the economy will work better and there will be less need for intrusive regulation of market conduct, if a more competitive structures can be recreated.

Third, while it goes against my grain as an advocate of competitive markets, it is essential to have more direct regulation of the market process in agriculture. The present structural situation on both the supply and buying sides has fostered a wide range of highly undesirable and anticompetitive strategic behaviors. To restore the balance necessary for workable markets and

ensure that the long run dynamic capacity of all participants is not destroyed, it is essential that market facilitating regulations exist. Those regulations need to ensure that market conduct is as transparent and non-strategic as possible. Such regulation should limit or eliminate manipulation of market price variables, require good information including full disclosure of past and present transactions as well as forward looking commitments. Some contracting requirements should be per se illegal–they have no real use except as strategic devices. My further suggestion is that drafting such market facilitating regulation requires market specific expertise and often substantial discussions between representatives of buyers and sellers to formulate effective and minimally intrusive regulations. The role of the legislature is to define the ultimate goals for such a process and to authorize an appropriate agency to carry out the market facilitating regulatory function. The floor of the senate is no place to write detailed regulations for any industry.

One final note, the current focus of concern is largely on the selling side of agriculture. As I have reviewed both the structure and conduct of firms on the supply side, especially in the seed and herbicide area, I have come to the conclusion that the threat to competition presented by that side of the marketplace is very substantial. Building on existing regulatory concerns most of the current proposals focus exclusively or predominantly on the selling side. This is a serious omission.

In particular, the current scope of patentability and the range of rights that patent holders have obtained in the context of concentrated agricultural supply markets in which strategic behavior is very attractive is resulting in an increasing number of anticompetitive restraints on the use of new biotechnology. I would urge the committee to be attentive to these risks as well as the better known ones on the buying side.

Let me conclude by observing that robust, competitive markets have been and should remain the center of our economy. The failure to preserve and protect them will result in serious economic and social costs. This is true in general and with special emphasis in agriculture.

Concentration, Competition, and Industry Structure in Agriculture

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It is a pleasure to be asked to offer testimony on concentration, competition and the changing structure of agriculture and agricultural markets, and to participate in this panel. Concentration and competition are the area within which I have focused most of my thoughts and research program for much of my professional life. I have done this because I believe it is the most important economic and public policy issue that faces U.S. agriculture.

However, it has been intriguing to me to observe the interest with which agricultural producer groups, industry associations, and government bodies place on the issue of concentration and industry structure over time. Public interest in this topic waxes and wanes with profitability in the various industry sectors. It is my perception though that the underlying economic forces at work determining this change have remained largely constant. This illustrates to me the need for the impartial academic university perspective. Further, these economic forces have been with us for many years – since the 1840s with the emergence of international trade and industrialization of agricultural production and marketing. The process of industrialization has ebbed and flowed with scientific technological advancement, but the course of change has been steady. It appears to me that the *issue of industry structure* always seems to become **The Issue of Industry Structure** following time periods of increased production, low prices, and low profitability. It is my perception that this is what we have today.

It is not my intent to make light of the issue or the recent income problems the farm sector has faced. Price and profitability declines have been substantial for a number of commodities and sectors since the peaks of 1996. Further, the declines have been widespread through a large number of high-volume commodities. But it is clear to me that the cause of this problem is supply and demand related, and is not due to industry structure. On the supply-side, there has been exceptional weather, increased crop production, and increased livestock production. On the demand-side, the relief-value that exports provide for the domestic markets has been limited because of the strong U.S. dollar, the sluggish world economy and the weak Asian country economies in particular. Industry structure is not the devil it is often portrayed. I think that it has had little impact on markets in the recent years. For example, there has been little increase in concentration within livestock processing – the markets I follow most closely – since the late-1980s.

Concentration is not the cause of low prices and profitability in agriculture. However, there are a number of specific issues which have arisen out the continued consolidation. There are serious questions about market access for independent producers, market entry for firms with innovative ideas, service of the general public interest by large businesses, and policy inconsistencies which have contributed to increased consolidation and concentration.

April 25, 2000

The issue of industry structure is important. Study of this area is the one constant in my career. It is important to outline the economic concepts at play and it is important to take a comprehensive look at what the published research has to say about this issue.

Long-Term Perspective

Competitive markets require many buyers and sellers combined with an open exchange of market information. Lawmaking government bodies and regulatory agencies face a dilemma referred to by economists as the Williamson tradeoff. Growth and consolidation among firms happen for a reason. It is due to enhanced technical efficiency and reduced costs associated with production, processing, and distribution of products within an industry consisting of large firms. However, the resulting concentrated structure may facilitate noncompetitive behavior among the few remaining firms, leading to net social costs in terms of higher consumer prices and lower prices for producers. The issue of this tradeoff is particularly relevant in U.S. agricultural processing industries – and specifically livestock and meat industries.

However, this question could also be asked of about any sector in production agriculture – this includes livestock, poultry, grain crops, and fruits and vegetables. One of the more important pieces of information that can be gleaned from the *1997 Census of Agriculture* is the degree of concentration in agricultural production. It is common that more than 80% of the value of production within an industry is produced and marketed by less than 20% of the producers.

The research community has recognized the need to evaluate the potential tradeoffs between economic efficiency and abusive market power. However, it has been almost exclusively focused on agricultural marketing and food processing industries. Research has been motivated by the desire to protect farming and rural community interests. There is a large body of academic literature devoted to this topic. There are a number of research programs, academic programs, and academic professional organizations that are devoted to discovery and communication on this issue. (These groups include NE-165 and The Food and Agricultural Marketing Consortium.)

The interest in market structure has not always been substantial – especially in the policy arena. In the economic and political climate of the early-1990s, where the national emphasis is on economic development and job creation, research on market structure topics was difficult to fund and difficult to publish.

We should not lose sight of the long-term economic goal of maintaining competitive markets. Research and policies need to facilitate economic growth, but also need to identify and encourage the right kinds of economic conduct. We should be cautious of changes which may lead to larger economic problems in the future. However, we should not limit change because it is unpopular or painful. Economic growth and change are often painful for a few but beneficial to the nation and economy as a whole.

What Does the Research Say?

Much popular press hay is made from the increasing nominal and real value of the marketing bill, or the widening gap between retail-level and farm-level prices. The widening of this gap is almost entirely due to the increasing cost of marketing services. Consumers are purchasing more and more service, demanding increases in quality and variety, and desiring more and more convenience. All declines in the farm share of the consumer's dollar is due to the farm and ranch providing less and less of the final product with which the consumer is interested.

Profitability of farm product processors and marketers are remarkable in size – remarkable in how small they are and how consistently small they are. The profits of firms which provide food-related goods for at home consumption are 4-4½ % of consumer expenditures, or business income, net of the value of the farm input. Profits are 4-4½ cents on a dollar of net margins with the remaining 96-95½ cents going to cover costs.

The real proof-in-the-pudding emerges if you look at the stock prices for these firms. Financial markets absolutely recognize the profit limitations of agricultural marketing and food processing companies. The stocks of these companies are clearly priced as slow-growth low-profit businesses.

Much popular press hay is also made from the high levels of concentration in agricultural marketing and food processing industries. The causes of the concentration are economies of size, scale, and scope. Large facilities, large firms, and concentrated industries have lower costs. Low costs translate into larger sectors – aggregate supply is larger – lower prices for consumers and higher prices for producers which supply the farm-level inputs. The tradeoff is clearly that concentrated industries have a greater potential for exercise of market power.

Livestock and grain processing and marketing has become dominated by large plants and firms. A series of mergers and acquisitions in 1987 involving some of the nation's largest meatpackers, combined with internal growth by the largest meatpacker, resulted in what has since been called the "Big Three" packers. As a result, concentration or market dominance by a few firms has increased to unprecedented levels. Fewer and larger meatpackers have resulted in increased plant and industry efficiency. However, several studies suggest larger meatpackers have exercised market power in livestock procurement. Fewer buyers and increased concentration and consolidation lead to lower prices for livestock. There is little evidence about the effects of concentration on consumer prices. While research points toward the conclusion that larger meatpackers have exercised market power, many researchers interpret the results as inconclusive. This was also a conclusion of the 1990 U.S. GAO review of available research. This report was instrumental in initiating the P&SA Concentration Study mandated by Congress.

At the same time, studies of livestock processing industry costs clearly show these costs are substantially lower for large firms and that these benefits result in higher livestock prices. The bottom-line of published research is that the gains to efficiency of large firms are greater than losses attributable to the exercise of market power. In the case of beef slaughter and processing,

the cost savings are approximately 4-6% of price levels while the losses due to market power are approximately 1-2% of price levels. Efficiency gains are in most cases orders of magnitude greater than market power losses.

What Does the Research Not Say?

Industries continue to innovate and change. There are always new but-what-ifs. Likewise, the economics profession develops new models to study conduct and measure the impact on economic performance. We need to look ahead and continue to be vigilant, but we also need to be scientific and discuss what we know as the truth no matter how unpopular it is.

Livestock slaughtering and grain processing industries have become dominated by large plants and firms. Specifically, meatpackers have changed the manner in which they purchase livestock, increasingly using contracting procurement methods: (1) packer feeding of livestock in packer-owned facilities or on a custom basis; (2) forward contracting or production contracting; and (3) purchasing livestock under exclusive marketing/purchasing agreements. Such structural and behavioral changes affect the economic performance of firms and industries. Economic performance measures include efficiency, profitability, productivity, and investment in research and development, among others. Much is not known yet about behavioral change impacts on competition and pricing and further research is necessary. There has also been little study on long-term productivity, investment in research, and product development.

Policy Inconsistencies and Opportunities

I see a number of inconsistencies in farm and economic policy that have, in part, lead us to where we are today. U.S. government bodies have spent considerable time addressing what to do about the economic viability of the family farm and ranch. Many farm-related government programs have this in mind. The legislation under consideration currently addresses this issue by cracking down on concentrated industries and the exercise of market power. But there is little evidence of market power. This legislation also attempts to limit unfair practices. But what are unfair practices? Defining unfair is the precise problem with the P&S Act. Limiting unfair trade practices is an almost hopeless and certainly expensive path. The proposed legislation will not change the margins, marketing bill, or the farmer's share of the consumer's dollar.

What can be done? What are the opportunities? First, legislation should focus on the limitation of market access and protection of market entry. Contract production is mainly motivated by quality and cost management problems. Legislation needs to look at limits to access of participation in contract and other integrated systems.

I can also envision an economy which is better served by 12 firms in a particular processing industry than it is by four. Beef demand has declined substantially since the early-1980s and the cause is linked to quality, consistency, and convenience of consumer products. This structural change is well known. Yet it is only recently that the processing industries have made any

significant efforts to address this problem. Until now, the existing firms have focused on doing the same things that they had been doing for years only at larger volumes and lower costs. New industry entrants have been driven out and innovation is difficult. I wonder how much larger the beef production industry would be – with its base in rural America – and how much better consumers would be served if the beef processing industry consisted of a larger number of smaller and more innovative firms.

Second, legislation should provide for public goods. Public goods are those things that the marketplace does not provide enough of for various reasons. I am a strong believer that well-reported and open marketplaces are public goods. There is currently significant support for mandatory price reporting and yet in the late-1980s and early-1990s the funding of Livestock and Grain Market News within the USDA Agricultural Marketing Service was reduced. The justification was that private news reporting services would provide this function. That has not happened because of the public good component. I do not think mandatory price reporting will do as much for agricultural markets as simply increasing the funding to AMS would.

Further, the government should support development electronic trading mediums. This was done in the late-1970s and early-1980s and the competitive properties of those institutions were well documented. However, most of the systems failed commercially because of their costs. Since then, there have been quantum improvements in that technology and reductions in costs. But there are few systems currently under development because of the public good component.

Third, legislation should support the public institutions that are difficult to change but that are essential to the operation of markets. Advancements need to be made in agricultural commodity grades and standards and supporting technologies. These technologies then need to be implemented. A large portion of the increase in contract production is because quality control is impossible without it. I would argue that little contract production has emerged because of power. It has emerged to produce a product more consistent with low-cost processing systems and consumer wants. The beef industry has needed a scientific method of measuring tenderness of a carcass and a system to implement that measurement at commercial processing plant speeds. Investment in this technology would help the independent beef producer.

I believe that we are currently in the throes of a large market failure – that being increased consolidation, contracting, and vertical integration – not because returns to power are so great but because of our collective failure to protect innovation and invest in public goods and the market institutions that are necessary for a competitive marketplace populated by independent producers.

Thank you again for the opportunity to speak.

April 25, 2000

NATIONAL CATTLEMEN'S BEEF ASSOCIATION

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Testimony

on behalf of the

NATIONAL CATTLEMEN'S BEEF ASSOCIATION

in regard to

Pending Legislation on Agriculture Concentration and Competition Issues

submitted to

Senate Committee on Agriculture, Nutrition and Forestry

The Honorable Richard G. Lugar, Chairman

submitted by

John Greig
Estherville, Iowa
National Cattlemen's Beef Association

April 27, 2000

Initiated in 1898, the National Cattlemen's Beef Association is the marketing organization and trade association for America's one million cattle farmers and ranchers. With offices in Denver, Chicago and Washington D.C., NCBA is a consumer-focused, producer-directed organization representing the largest segment of the nation's food and fiber industry.

Statement by John Greig, Estherville, Iowa
National Cattlemen's Beef Association (NCBA)
Senate Committee on Agriculture, Nutrition and Forestry
Pending Legislation on Agriculture Concentration and Competition Issues
April 27, 2000

Thank you Chairman Lugar, Senator Harkin and Members of the Committee for holding this hearing to discuss pending legislation on agriculture concentration and competition issues and related issues of concern to cattle producers. NCBA commends your leadership and continuing efforts to examine the ongoing and dynamic changes in beef cattle industry and for working with us to find ways to improve our ability to more effectively market U.S. beef. I am John Greig, President of Greig Company, a diversified farming and cattle feeding operation from Estherville, Iowa, past president of the Iowa Cattlemen's Association and a member of NCBA.

NCBA and the 250,000 cattle producers we represent are encouraged by the open and honest discussion of the issues facing the livestock industry. Today's hearing provides the opportunity for discussion and debate on these issues, which is vital to the democratic policy development process -- both within NCBA and to the nation at large. As evidenced last year, such debate afforded our producers the chance to work with members and staff of this committee to improve availability of market information and enhanced competitiveness through market forces. As we await the implementation of the new price reporting law, we again thank you for that initiative.

A Changing Industry:
As with your hearing in early February, this hearing is a continuation of the ongoing process to closely examine the marketing structure changes occurring in the livestock industry and the concerns of livestock producers seeking to maximize their returns in a very competitive domestic and international marketplace. There is a broad range of opinions among cattle producers about the effects on the beef industry of new marketing systems and structures, international trade agreements and packer concentration/competition.

The structural changes taking place in our industry have coincided with volatility in international economies, changes in supply, improvement in beef demand and tough market conditions for feed grain and forage producers, and are the basis for heated debates and general consternation by virtually livestock producers. Some individuals have embraced new marketing structures and systems for their own advantage, while some believe they are, at least in part, responsible for the price declines during the mid to late1990s.

As USDA data shows, the four largest beef packers slaughter approximately 80 percent of all steers and heifers marketed, which has not changed appreciably since 1990. Nonetheless, NCBA supports close monitoring of mergers and acquisitions and aggressive enforcement of antitrust laws and regulations to ensure a fair, competitive marketplace for all participants. We also support thorough evaluation of price movements and margins to assure that price changes are the result of market signals and not the exercise of market power or illegal pricing activities. To this end, the new price reporting system developed by this Committee will provide additional data to aid in this process.

The toughest challenge is to remain pragmatic as these issues are analyzed. USDA's GIPSA has conducted several investigations, both broad and focused, relative to the beef industry structure and marketing practices, and has taken enforcement actions when necessary to address infractions.

However, repeated anti-trust investigations by GIPSA and the Justice Department have not uncovered broad, industry-wide illegal activities. Part of the frustration in the country is that many marketing practices and industry concentration levels that are perceived to be illegal are not.

NCBA supports cooperative efforts by USDA and Justice to ensure that marketing practices and mergers and acquisitions that could lead to further concentration in our industry are closely monitored and examined. We also would encourage USDA to assist Justice in their anti-trust efforts by providing data on the impact of these activities, especially in areas where Justice officials may not have ready access to such data.

In addition, NCBA has long supported strong oversight and enforcement of existing anti-trust and market protection laws. NCBA's 1988 Beef Industry Concentration and Integration Task Force spent a year evaluating this issue in anticipation of ongoing industry restructuring. The GAO has conducted repeated studies going back to the 1980s including "Beef Industry Packer Market Concentration and Cattle Prices," December 1990 and P&SA Oversight of Livestock Market Competitiveness Needs to Be Enhanced," October 1991.

These and other studies coupled with industry input have resulted in GIPSA restructuring and modifications in enforcement and investigative activities. The studies also could lead one to conclude that oversight and enforcement of anti-trust laws and market protection initiatives would benefit most from additional funding to ensure there is adequate personnel and resources to bolster these efforts.

Change in the beef industry, as in the rest of the economy, is a reality. The global market is a reality. And these realities have necessitated changes by cattle producers and other sectors of our industry to maintain competitiveness in the international marketplace. Efforts to inhibit or roll back change in the cattle/beef industry will only result in policy-imposed inefficiencies and decrease competitiveness. This is especially true if other U.S. meat and poultry industries, not to mention foreign beef producers, have the freedom restructure and modify marketing practices to meet the needs of the changing marketplace.

Simply put, we support more competition, not less. How the beef industry achieves this goal is a major challenge. There are indications that new processors and alliances are poised enter the beef industry. "Quality Beef," an alliance of producers and a major U.S. retail firm formed to supply specification branded products to consumers has announced plans to open a state-of-the-art packing plant in Kansas with a future goal of adding an additional three processing plants. The objective of this system is control quality and product safety from "DNA to Dinner." To encourage and increase additional packer competition, we must first examine the barriers that inhibit entry into fed cattle beef packing and assure that legislative and regulatory restrictions do not inhibit innovation and investment.

Smaller plants that currently operate under state-inspected programs are currently prevented from taking advantage of expanding their markets if it would require interstate shipment of their products. To do so, they must first make the necessary, and often expensive, steps to become federally inspected. NCBA recommends that meat inspected under state programs should be accorded the same freedom of movement in interstate commerce that is accorded foreign-inspected imported meat.

NCBA recognizes the Committee is considering legislation in this regard and appreciated the opportunity to testify at the Committee's recent hearing on interstate shipment. Again, we commend you and your colleagues for your leadership moving this initiative forward. We are anxious to work with the Committee, your counterparts in the House and the Administration in identifying and addressing other conditions and/or constraints that inhibit an increase of participants in the packing and processing sector.

New Marketing Systems:
An increasing trend in the beef sector are the alignments between packers and cattle producers through alliances, joint ventures, cooperative agreements, contractual and formula arrangements, and custom feeding of packer-owned cattle. NCBA policy is specific regarding these emerging business relationships.

- NCBA will not recommend the limitation of any method of marketing fed cattle.
- NCBA supports a free market system.
- No action is to be taken to alter or halt current trends toward private business arrangements among operators in the various sectors of the beef industry.
- NCBA is to encourage producers -- individually and through cooperative efforts -- to take advantage of opportunities to increase profits through new marketing strategies, coordination, risk management and retained ownership.

A number of producers are finding innovative ways to compete in the changing beef industry including gaining a greater share of the marketing dollar. There are several examples representing different approaches by groups of cattle producers, such as:

- U.S. Premium Beef, Ltd.
- Western Beef Alliance
- Ranchers' Renaissance
- Iowa Cattlemen/Excel joint venture
- Angus Alliance
- Five-State Beef Initiative
- Harris Ranch
- Nichols Farms Alliance

These are just a few of the innovative marketing systems available. There are many more, particularly in areas where producers are teaming with other segments of the industry to take advantage of national, regional and/or niche market opportunities. A unique opportunity is evolving in my home state of Iowa as follows:

A Memorandum of Understanding was signed by Iowa Cattlemen's Association (ICA), Excel and the State of Iowa on October 27, 1999 to finalize a feasibility study for constructing a new beef packing plant in Iowa. The agreement originally had a February 28, 2000 maturity date, but by agreement from all parties, has been extended 90 days. Under the agreement the Iowa Cattlemen's Association will be responsible for securing minimum commitments from cattle producers for the 200,000 head (40%) of committed cattle required for this facility. These producers are also to become members of the Iowa Quality Beef Supply Network (IQBSN), who will be the partner with Excel on this project. Currently, IQBSN has approximately 925 members from 98 of Iowa's 99 counties and 12 other states and more than 330,000 cattle commitments have been received.

Excel will furnish estimates of staffing needs for the project, engineering specifications for the site including highway and rail access, water supply and wastewater discharge, project development costs, as well as cattle purchasing and beef marketing strategies.

The State of Iowa, through the Iowa Department of Economic Development (IDED), will continue to work closely with ICA and Excel in providing labor availability assessments, coordinating community involvement and working with other state and local government entities in the site selection process. In addition, IDED is assisting in funding mechanisms and legislative and regulatory issues.

The $100 million dollar plant will focus on high quality, high yielding cattle that perform well under the Beef Quality Assurance and Beef Safety Concerns. The plant will utilize the latest in technology, including tracking electronically identified (EID) cattle through the plant visual scanning system and other new technologies. The plant will have 1,100 employees on a single shift, with the potential to expand to a double shift of 2,200 employees. Approximately 637,500 animals will be processed annually, with the potential to increase that number as the plant size increases.

The Iowa Quality Beef Supply Network is the producer investment arm of the facility created to secure annual commitments of approximately 40% of the plant's capacity, for five years. In order to become a member, producers have paid a registration fee of $500 and a $2 per-head delivery fee pre-payment, as well as join their state cattlemen's association. Cattlemen who joined IQBSN prior to December 31 are considered founding members. The membership opportunities are still open and IQBSN is accepting increases in cattle commitments. In addition to conventional financing options for producers through their individual lenders, three new financing programs have been announced to assist cattlemen in financing their final delivery fee prepayments,

An interim grid is now available to members of the Supply Network for those cattle that are EID tagged, through the Iowa Quality Beef program. This grid is for the Schuyler, NE, Excel facility and is limited to 2,000 head per week from these sources. During the month of February, 1,500 head of cattle were sent and received an average premium of $24/head.

These innovators are long-term professional cattlemen who came together in a proactive way to address their desire for a growing, viable beef industry through bold new marketing strategies that enable them to capture a larger share of the retail beef dollar. No longer are these producers' energies consumed by concerns about market structure. Their efforts revolve around producing a better beef product marketed through their own beef company at their direction. As owners, these cattlemen receive rewards from a value-based pricing system, individual carcass data and earnings from the company at year-end. In addition, the data received by cattle producers from these efforts enable them to continuously improve the quality of their livestock, which in turn can lead to additional market returns.

It is critical that Congress ensure that legislative and regulatory policies continue to encourage these types of solutions and do not limit a producer's ability to gain a greater share of the marketing dollar. Much of the discussion and debate among thought-leaders in the industry has been about how to foster new marketing systems that meet consumer needs and increase beef demand. While we recognize the concerns that have lead to development of proposals regarding industry structure and competition, NCBA remains concerned about unintended consequences and urges a thorough analysis of the potential impacts of these proposals.

As we noted earlier, the Committee followed such a process in developing the mandatory price reporting legislation to ensure it would increase information flow and market transparency without unintentionally placing new and innovative marketing systems at a competitive disadvantage. Clearly, there is widespread agreement that efficient markets require greater market transparency that is achieved by the availability of accurate and timely information -- especially in situations with many sellers and few buyers. Information availability helps ensure that competitive market forces exist and that few buyers do not have undue leverage when market information is widely available to more dispersed sellers. With this in mind, we encourage the Committee to follow the example it set last year in determining how to best proceed on the proposed competition bills.

On-going Industry Evaluation:
NCBA remains committed to addressing changes in the industry structure and the underlying economic forces driving those changes. Over the years, NCBA and its predecessor organization have devoted considerable financial and human resources to examine our industry and educate cattle producers regarding these issues. Following are examples of some of the major initiatives:

1. Rapid changes in the number, size and make-up of firms in the beef industry and shifts from traditional ownership and marketing patterns raised many questions about the future structure of the beef industry during the mid-1980s. Concerns were raised about the competitive position of beef relative to other meat sources domestically and internationally and how individual producers might adapt and fit into the evolving structure. The NCA (predecessor to NCBA) Beef Industry Concentration/Integration Task Force was appointed October 6, 1988, to address these issues, questions and concerns. Task force members represented all geographic areas and all segments of beef cattle production. The final task force report projected many changes that are now under discussion and identified the competitive economic forces that would drive the industry to change.

2. The NCA Beef Industry Concentration/Integration Task Force also requested that a group of experienced professionals take an "arms length" look at some of the difficult issues facing the U.S. cattle industry. The report, "*Competitive Issues in the Beef Sector: Can Beef Compete in the 1990s?*" addressed competitive forces in the domestic and international markets that would lead to increasing change in the U.S. beef industry. The analysis was conducted by an elite team headed by D. Gale Johnson, University of Chicago and G. Edward Schuh, Humphrey Institute of Public Affairs, University of Minnesota. Other research team members included John M. Connor, Purdue University; Timothy Josling, Stanford University; and Andrew Schmitz, University of California, Davis, all recognized leaders in their respective areas.

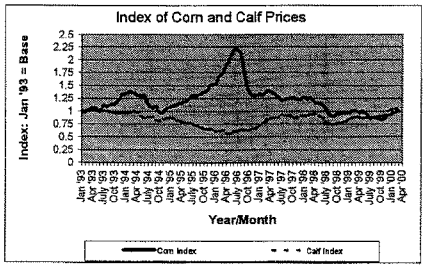
3. In response to many of the competitive issues raised in the above reports the beef industry began to evaluate the prevailing cattle and beef marketing systems at the time. The Value-Based Marketing Task Force was a joint effort by NCBA predecessor organizations released its final report in August 1990. The task force recommended changes in the beef production/marketing system that would better align the production and merchandising practices of cattlemen, packers, purveyors and retailers with the beef product preferences of consumers. The task force determined that consumer needs could be better targeted simultaneously with cost reduction if the industry would reduce waste fat production.

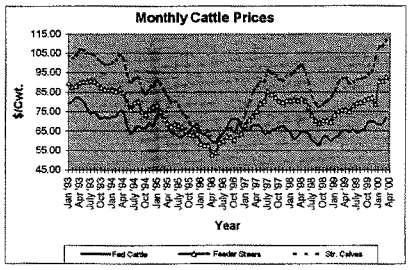
4. The beef industry was slow to adopt recommended changes and beef continued to lose market share. In 1993, the Long Range Planning Task Force recognized the decade of the 1990s as a time of challenge and change for the beef industry. The long-range plan was adopted by the major beef industry organizations. Organizational restructuring was undertaken with the primary objectives of increasing beef demand consistent with the vision statement and objectives of the Beef Industry Long Range Plan.

These private sector initiatives have been supplemented by the extensive 7-part analysis of Concentration in the Red Meat Packing Industry competed by the Packers and Stockyards Administration in 1996 followed closely by the USDA Advisory Committee Report on Agricultural Concentration.

Improving Market Conditions:
The beef industry and other livestock sectors are in many ways a bright spot among many depressed agricultural commodities. In part, this is because we have resisted asking the government to "fix" industry conditions caused by market forces. It is our hope that through this backdrop, it may be easier for the Committee to understand why there is a great deal of caution and reluctance among cattle producers to call for dramatic expansion of government intervention in the beef industry marketplace.

We do empathize with current low prices experienced by grain producers. It is only recently that beef demand improvements have boosted prices for calves and yearlings, enabling cattle producers to begin recouping losses incurred during our own market crisis that began in early 1996. Prices for all classes of cattle are significantly improved from the cyclical lows established during 1996, and prices for calves are now higher than cyclical high prices of the early 1990s. During March and April 1996, the monthly average prices for steer calves averaged less than $60/cwt. and feeder cattle prices averaged less than $54/cwt. These prices were a major decline from prices experienced during the late 1980s and early 1990s and were directly related to cyclical increases in cattle numbers and record high grain prices during the mid 1990s.





Conditions have improved dramatically since the doldrums of the mid-1990s. Prices for steer calves have generally ranged above $90/cwt. since January 1999 and averaged record high prices during the first quarter of this year. Fed cattle prices averaged nearly $70/cwt. during November 1999 and are currently in the mid-$70s/cwt. Higher cattle prices are primarily due to declining numbers of calves and feeder cattle, improving beef demand after a 20-year decline, improvements in Asian financial conditions resulting in improved beef demand and by-product values and general improvement in export markets.

As stated at the outset, of this testimony NCBA and the beef industry support Justice Department and USDA enforcement of the Packers and Stockyards Act (PSA) as amended and other anti-trust laws and regulations. We support timely and complete USDA implementation of mandatory price reporting legislation passed last session. We urge that USDA be involved in pre-merger evaluation of proposed packer mergers in coordination with evaluation by the Justice Department and support adequate funding for GIPSA and the Justice Department to accomplish their investigative functions.

NCBA supports a free market system and we trust in the ability, adaptability and innovating skills of the US cattleman to be able to prosper in a relatively unregulated domestic and international marketplace. We rely on federal regulators to ensure that the marketplace is free from anti-trust, collusion, price fixing and other illegal activities that damage the viability of the market and interfere with market signals, but also to keep the playing field level for cattle producers. If allowed to work the market will recover with a minimum of government intervention and cost of regulatory inefficiency. To remain competitive in a global market, this is absolutely a necessity.

We are prepared to work with you and your staff to provide additional information and direction. Again, we certainly appreciate the leadership the Committee has shown in addressing the tough issue of an evolving competitive industry structure and the appropriate role of government oversight.

Thank you for the opportunity to present this information.

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Testimony of

Jon Caspers
National Pork Producers Council

Before the

Committee on Agriculture, Nutrition and Forestry
United States Senate

Concerning

The Impact of Agribusiness Concentration
On Producers and Consumers

Presented

April 27, 2000
Washington, DC

National Headquarters
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The Other White Meat:

Mr. Chairman and Members of the Committee:

My name is Jon Caspers. I am a pork producer from Swaledale, Iowa and serve on the Board of Directors of the National Pork Producers Council (NPPC). Today, I am representing America's pork producers and am pleased to discuss with you the critical issue of agriculture concentration and its impact on pork producers and consumers. Agricultural concentration is a difficult and emotionally charged issue. Many pork producers are concerned about their ability to continue to compete and maintain market access in a hog market that is experiencing increasing levels of concentration.

Changing Pork Industry

Global competition, new technologies, and consumer demands are but a few of the factors that are rapidly changing the U.S. pork industry. Hogs are raised differently today than even just 20 years ago. Hog farms are managed in new and innovative ways. Hogs are marketed on a carcass weight-carcass merit basis verses the traditional live weight selling in the past. Both producers and the packing industry are vastly more efficient but much less flexible than in the past. Coordination of the production and processing chain with consumer demands is more and more critical to the success of all industry participants, but perhaps most critical to the future of producers.

Pork Industry Concentration

The pork industry is becoming more concentrated at every level, yet we continue to be less concentrated than the poultry industry or other livestock sectors. Consider these statistics:

Packing concentration: Concentration in the pork packing sector as measured by the 4-firm concentration ratio has grown from 32.2 percent in 1985 to 56.3 percent in 1998. Smithfield, IBP, Swift and Excel are the firms currently included in this measure of total market share. The eight-firm concentration ratio now stands in excess of 75 percent. While not a guarantee of conduct that increases consumer prices and/or reduces producer prices, these levels and their trends increase the possibility of such conduct and provide ample incentive for heightened vigilance.

Production concentration: Concentration in the production segment has grown from negligible levels in the early 1980s to about 18 percent following the recent acquisition of Carroll's Foods and Murphy Family Farms by Smithfield Foods. The four-firm ratio cited here includes the market shares of Smithfield, Premium Standard Farms, Seaboard and Prestage.

Vertical Integration: Vertical integration of packers owning hogs has grown from an estimated 6.4 percent in 1994 to roughly 24 percent today. Smithfield, Premium Standard Farms, Seaboard, Excel, Lundy and Farmland are the companies contributing the most to this total.

Hog Marketing Contracts: As recently as 1994, 71 percent of the hogs were sold on the spot market and only 20 percent were sold using a price formula. In January 2000, 74.3 percent were non-spot market purchases and 25.7 percent were spot market purchases. This trend has reduced the size of the negotiated hog market substantially and caused many concerns about the efficiency and accuracy of the price discovery process in use today.

Enhancing Market Competitiveness

In the last few years, NPPC has launched a number of new initiatives to help ensure that pork producers have a fair, transparent and competitive market for their hogs. Most of our efforts have focused on obtaining and disseminating more (and more accurate) information to producers and improving producers' abilities to make knowledge-based business decisions based on that information. Though more difficult and time consuming than legislation or regulation, we firmly believe that information and knowledge will be the main basis for long-term solutions to potential problems of competition in markets, especially in global markets for meat, protein and food.

A large number of these initiatives were designed and implemented by a broad cross-section of pork producers who serve on NPPC's Price Discovery Task Force which I currently Chair. These major initiatives included:

- Development of a packer price reporting system that focuses on actual procurement costs. Farmland Foods began participating in this system in the fall of 1998. It continues today.
- Passage of the Mandatory Livestock Price Reporting Act of 1999.
- The NPPC Producer Price Reporting initiative which encourages producers to negotiate their free supplies of market hogs with more than one packer and to report the price to USDA.
- Recent publication of the "Guide to Marketing Contracts" whose goal is to help producers make more informed decisions about marketing contracts and their terms. This guide updates previously-published guides to production contracts and pricing of early-weaned pigs (which is currently being revised),
- NPPC conducted, with the University of Missouri, comprehensive live hog marketing studies in 1999 and 2000.

In addition, NPPC facilitated the creation of a national producer-owned cooperative called Pork America. Pork America's goal is to find new

opportunities for producers to participate in and capture value from the pork chain beyond the farm gate. Producers are interested in this activity because of the growing proportion of the consumer pork dollar that goes to the value-adding activities of the marketing sector and because of the success of producers in cooperatives in other countries such as Denmark. Danish pork producers control their own fate because they now own virtually all of their country's pork production and processing industry.

The recently-announced closure of the Farmland Foods packing plant in Dubuque, Iowa puts U.S. daily slaughter capacity at about 380,000 per day; very near its level during the disastrously low prices of the fall of 1998. As the U.S. pork industry contemplates the need for new, efficient pork packing and processing capacity within the next 5 years, producers believe that effective competition from producer-owned entities or alliances may be another antidote to the tide of concentration in the pork-marketing sector.

Agriculture Concentration Issues

Until information systems are fully operational, the ability of producers to use the information is increased and producers become more involved as competitors in the marketing/value adding system, concerns about concentration and its potential for non-competitive conduct will remain. Concerns such as these led producer delegates to the recent 2000 National Pork Industry Forum to consider several agriculture concentration resolutions from member states and pork producers. After considerable discussion and debate, producer delegates agreed to support the following positions on agriculture concentration and market regulation issues. They include:

1. USDA Hog Market Structure & Competitiveness Study – The Department of Agriculture should conduct studies on hog market structure and competitiveness issues within the pork industry, outlining present realities, future scenarios and the implications for producers' economic wellbeing and our nation's food supply.

2. Price Discrimination -- The definition of price discrimination should be clarified, a prohibition on price discrimination should be established, and the Secretary of Agriculture's authority to challenge price discrimination should be reiterated.

3. USDA Study of Justifiable Price Differentials – The Department of Agriculture should study the factors that comprise economically justifiable price differentials, including factors such as volume, time of delivery, carcass specifications, etc.

4. Study of DOJ Concentration Threshold Levels -- A study should be conducted of the threshold levels of standard concentration measures

(Herfendahl-Hirshman Index, Concentration Ratios, etc.) which are used by the Department of Justice to trigger scrutiny or investigation of the livestock and livestock slaughter sectors. We believe the study should focus on the current threshold levels, why they are used and whether they are applicable to a highly perishable product such as livestock.

5. Adherence to Antitrust Laws – Continued scrutiny of the packing and processing industry on the national level to assure adherence to relevant federal antitrust laws.

6. New Antitrust Laws -- New antitrust laws should be considered that ensure opportunities for independent hog producers.

7. USDA Merger & Acquisition Reviews -- The Department of Agriculture should be given new authority to recommend to the Department of Justice approval or disapproval of agricultural mergers, acquisitions and consolidation of agricultural input suppliers and processors and sufficient funding to properly discharge these activities.

8. USDA Corporate Structure Report -- The Department of Agriculture should be given new authority to require agribusinesses with more than $100 million in sales to annually file information related to corporate structure, strategic alliances, joint ventures and the like. The Department would publish a corporate structure report based upon these data.

9. Deputy Attorney General for Agriculture -- A Deputy Attorney General for Agriculture position should be created at the Department of Justice.

10. Packers and Stockyards Act Enforcement – Press for aggressive enforcement of the Packers and Stockyards Act prohibition of discriminatory practices under current authority.

11. Packer Ownership – Pork producers recognize a packer's right to own swine and oppose any current legislation that restricts or limits alliances, cooperatives, ownership or joint ventures. Producers also oppose any legislation that differentiates the pork industry from other protein species with regard to alliances, cooperatives, ownership or joint ventures.

12. Producer Bargaining Rights – Endorse the concept of new legislation that requires processors to bargain with producer cooperatives.

Summary

NPPC realizes that guaranteeing U.S. agricultural producers a fair, transparent and competitive market for their products is a huge and continuing challenge. NPPC is ready and willing to work with you and the Committee on agriculture concentration issues. We hope that the Committee will approach this important issue using the highly successful formula employed on issues like mandatory price reporting and the interstate shipment of state inspected meat.

I hesitate to stress this cooperation point because neither Congress nor the Administration has yet to provide the remaining $1.35 million for the Mandatory Livestock Price Reporting Act to ensure that USDA can carry out its full legislative mandate in a timely manner. Funding for monthly Hogs and Pigs Inventory Reports, Improved Retail Price Data, and Swine Packer Marketing Contract Reports still has not been provided. This somehow must be done soon.

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

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

TESTIMONY of LELAND SWENSON
PRESIDENT of the NATIONAL FARMERS UNION

PRESENTED TO THE
SENATE AGRICULTURE COMMITTEE

HEARING ON CONCENTRATION

APRIL 27, 2000

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TESTIMONY OF LELAND SWENSON, PRESIDENT OF THE NATIONAL FARMERS UNION, PRESENTED TO THE SENATE AGRICULTURE COMMITTEE, HEARING ON CONCENTRATION, APRIL 27, 2000.

Mr. Chairman, Members of the Committee, my name is Leland Swenson, president of the National Farmers Union. It is an honor to be here to represent the 300,000 farm families who are members of National Farmers Union. I would like to thank you for scheduling the hearing today on pending legislation to increase competition in the agriculture sector.

Lack of market competition is a top concern of farmers and ranchers. I have traveled extensively across the country over the past year, and regardless of the size of the operation, the type of commodities produced, or the region of the country, price and concentration are the issues that raise the most concern about the future of farming and ranching. Let me repeat – price and concentration are the biggest issues in farm country today – bigger than trade, bigger than regulation reform, bigger than taxes, and bigger than crop insurance reform. The feeling in rural America is that mergers and acquisitions don't make the industry more efficient for independent family farmers and ranchers – just more dependant upon fewer buyers of agricultural production and fewer suppliers of agricultural inputs.

As you are aware, last year National Farmers Union commissioned a study on the impacts of agricultural concentration by Dr. William Heffernan, professor of rural sociology at the University of Missouri. I ask that the report, entitled "Consolidation in the Food and Agriculture System" be included in the record. Dr. Heffernan and his colleagues are now working on a follow-up study that will examine retail concentration and the related barriers to farmer-owned businesses competing in the market for value-added revenues generated by farm commodities.

The Heffernan study documented several major problems caused by concentration and consolidation, including: 1) how large firms are consolidating, forming joint ventures, or entering into marketing agreements to control the food and fiber supply from "gene to store shelf"; 2) how the resulting "clusters" have diminished the ability for price discovery as the clusters of firms control our food and fiber supply at every stage of production; 3) how the loss of family farmers is jeopardizing rural communities; 4) how environmental challenges are growing as a result of factory farms; and 5) the loss of bio-diversity occurring as companies move to standardization.

While the Heffernan study did a tremendous job of identifying what is happening in agriculture today, the question still remains as to what can be done to address the problems associated with the increased concentration. Mr. Chairman, there are bills currently pending before your committee that provide good starting points for addressing these issues.

Two recently introduced bills address the lack of competition in the industry--one by Senator Grassley, S. 2252, the "Agriculture Competition Enhancement Act", and the other by Senators Daschle and Leahy, S. 2411, the "Farmers and Ranchers Fair Competition Act of 2000". We strongly support these bills and hope that the provisions of both bills can be incorporated into one bill, reported by this committee and passed by the Senate before the Memorial Day recess.

In addition, we also support other legislation that is focused on addressing single issues, such as, Senator Tim Johnson's bill to limit packer ownership of livestock, and legislation by Senators Daschle and Hatch to allow for interstate shipment of state-inspected meat. Likewise, these bills deserve prompt consideration by the committee to help level the playing field for livestock producers and increase competition in the packing industry.

NFU POSITION ON S. 2252

S. 2252, introduced by Sen. Grassley, is a good start as it seeks to establish a Special Counsel for Competition Matters within the Department of Agriculture, provide for the review of agricultural mergers and acquisitions by the Department of Agriculture, and outlaw unfair practices in the agriculture industry.

It is important to have a point person in charge of competition at USDA to ensure that these issues receive the utmost attention. We believe it is critical to include the impact on farmers and ranchers when considering whether to allow a proposed agricultural merger.

NFU supports providing the opportunity for USDA to review pending mergers and acquisitions, with attention given to the impact the merger will have on agriculture. In order to make the review effective, the Special Counsel will need to be given both staff resources and statutory authority to file suit to prevent or restrict a merger. The authority specified in Sec. 4 (i) of the bill establishes the right to challenge a transaction in Federal court, although it does not provide details as to whether a failure by the Justice Department or the Federal Trade Commission to challenge a merger would weaken the Special Counsel's challenge. It also does not specify whether the Special Counsel would have the same authority as the other two agencies to challenge a transaction.

Another key section of the bill specifies a list of prohibited practices. This section can be strengthened by expanding the remedies allowed. Current language allows the Secretary to issue a cease and desist order and assess a civil penalty of not more than $10,000 per violation. However, the bill does not provide for restitution or compensatory damages to producers who suffered loss due to the violations.

National Farmers Union supports the provision in Sec. 6 that requires firms with annual sales in excess of $100 million to file a report with the Secretary of Agriculture.

We support Sec. 7 which prohibits confidentiality clauses in production contracts, and Sec. 8 which amends the Packers and Stockyards Act to provide greater protection for poultry growers. We also support provisions that authorize funding for the Special Counsel and increase funding for the Grain Inspection, Packers and Stockyards Administration to monitor and investigate changes in the meat packing industry and to hire litigating attorneys to enforce the law.

Finally, while we support Sec. 12 that establishes an assistant attorney general for agricultural antitrust matters, we note that the Justice Department has already created a similar position.

NFU POSITION ON S. 2411

We strongly support S. 2411, the Farmers and Ranchers Fair Competition Act of 2000, introduced by Senators Daschle and Leahy and others.

Sec. 4 of the bill prohibits anticompetitive practices and establishes a claims commission to provide for compensation for those injured by violations. We believe providing victim compensation is a vital part of the legislation. We are also appreciative of the whistleblower protection.

Sec. 5 requires the Secretary of Agriculture to conduct a pre-merger producer and community impact analysis for each proposed agricultural merger and prevents businesses from going forward without addressing potential violations identified by the Secretary. We strongly support those provisions as well as the provision that holds violators liable for treble damages.

We also support Sec. 6 which establishes minimum disclosure requirements for production and marketing contracts, including disclosure of responsibility for environmental damages. Disclosure provisions are becoming ever more important with the increased use of production contracts.

Sec. 7 requires agriculturally-related businesses that do over $100 million of business per year to report all strategic alliances, ownership in agribusinesses, and interlocking boards of directors and lobbyists to the Secretary of Agriculture. Sec. 8 creates a Special Counsel within USDA and authorizes hiring additional staff to implement the legislation. These provisions will assist USDA in better understanding, documenting, and responding to agribusiness concentration.

We are also pleased that Sec. 9 requires the General Accounting Office to conduct a study of farm-to-retail price spreads, as well as an analysis of the impact that formula contracts, marketing agreements, forward contracting, biotech patents, concentration in milk processing, and multinational mergers have on competition. Understanding these trends is essential to developing an effective response to restore strong and competitive markets.

In summary, while S. 2252 is a step in the right direction, S. 2411 is a much stronger bill that contains vital provisions that will be necessary if we are to restore market competition and revitalize our communities.

OTHER LEGISLATION

In addition to the two bills that focus on strengthening GIPSA and antitrust enforcement, there are two bills that respond to specific concerns within the livestock and meat industry. Senator Tim Johnson's legislation would make livestock markets more competitive by prohibiting packer ownership of livestock beyond the 14-day period prior to slaughter. This would prevent packers from flattening the demand curve by using their own cattle in times of increased demand.

Producers are extremely concerned about the price-depressing impact of packer ownership of livestock and other forms of captive supply. Yet, so far, USDA has been unable to effectively measure this impact. Prohibiting packer livestock ownership would help lessen the captive supply impact.

We are also very supportive of legislation to enable state-inspected meat to be sold across state lines. Since all plants now have to comply with the requirements of Hazard Analysis Critical Control Points (HACCP), we believe it is the right time to enact this legislation. The change will open up more choices to consumers and provide more markets for producers and small packing plants.

Again, thank you for the opportunity to testify today. There are many actions that Congress and the Administration can take to halt the rush of market consolidation. Attached is a list of 15 action items that National Farmers Union has recommended. A few are included in the proposed legislation. We look forward to working with Congress and the Administration to address these critical challenges.

ACTIONS RECOMMENDED BY NATIONAL FARMERS UNION TO ADDRESS CONCENTRATION

1. Enact a moratorium on agricultural mergers, acquisitions, and marketing alliances involving companies with gross revenues of $100 million or more, until Congress can review the impact these mergers are having on farmers, ranchers and rural economies.

2. Prohibit packer-ownership of livestock.

3. Provide funding necessary to ensure the implementation of mandatory price reporting legislation passed by Congress last year.

4. Require USDA to collect and report levels of concentration in all areas of agriculture including the production, processing, and supply industries.

5. Require firms seeking approval from the Justice Department (DOJ) or the Federal Trade Commission (FTC) for a merger or acquisition to disclose of all joint ventures, marketing agreements and strategic alliances.

6. Establish a level of concentration that triggers the presumption of an antitrust violation.

7. Require public disclosure of justification by DOJ and FTC whenever they determine mergers will not be challenged.

8. Require an economic impact statement detailing the expected impact a merger will have on net farm income of farmers and ranchers prior to approval by DOJ or FTC.

9. Require country of origin labeling of all meat and meat products.

10. Improve accountability of publicly funded agriculture research programs to ensure they are benefiting farmers, ranchers, and rural communities.

11. Prohibit the use of USDA rural development grants for creation of factory farms.

12. Pass legislation to bring poultry under the jurisdiction of USDA Grain Inspection, Packers and Stockyards Administration (GIPSA)

13. Pass legislation to allow contract producers to form collective bargaining units to negotiate with integrators.

14. Provide information, training, and financial assistance in the forms of grants and loans to foster the formation of cooperatives and other key small businesses in rural communities.

15. Prohibit slotting fees, i.e., the large fees charged to suppliers to put their products on the store shelves, to allow value-added cooperatives to compete at the retail level.

Statement of the American Farm Bureau Federation

TO THE
SENATE AGRICULTURE, NUTRITION AND FORESTRY COMMITTEE
REGARDING
CONCENTRATION IN THE
AGRICULTURAL SECTOR

Presented by:

Ron Warfield, President
Illinois Farm Bureau
Member, AFBF Executive Committee

April 27, 2000

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As the national voice of agriculture, AFBF's mission is to work cooperatively with the member state Farm Bureaus to promote the image, political influence, quality of life and profitability of the nation's farm and ranch families.

FARM BUREAU represents more than 4,800,000 member families in 50 states and Puerto Rico with organizations in approximately 2,800 counties.

FARM BUREAU is an independent, non-governmental, voluntary organization of families united for the purpose of analyzing their problems and formulating action to achieve educational improvement, economic opportunity and social advancement and, thereby, to promote the national well-being.

FARM BUREAU is local, county, state, national and international in its scope and influence and works with both major political parties to achieve the policy objectives outlined by its members.

FARM BUREAU is people in action. Its activities are based on policies decided by voting delegates at the county, state and national levels. The American Farm Bureau Federation policies are decided each year by voting delegates at an annual meeting in January.

STATEMENT OF
THE AMERICAN FARM BUREAU FEDERATION
TO THE
SENATE AGRICULTURE, NUTRITION AND FORESTRY COMMITTEE
REGARDING
CONCENTRATION IN THE
AGRICULTURAL SECTOR

Presented by:

Ron Warfield, President
Illinois Farm Bureau
Member, AFBF Executive Committee

April 27, 2000

Good morning, Mr. Chairman. My name is Ron Warfield. I am the president of the Illinois Farm Bureau and a member of the executive committee of the American Farm Bureau Federation. I have a farming operation in Gibson City, Illinois, and grow corn and soybeans. For 25 years, cattle feeding was also an integral part of my operation. Today, I am testifying on behalf of the American Farm Bureau Federation.

Farm Bureau believes that consolidation, and the subsequent concentration within the agricultural sector is having adverse economic impact on U.S. family farmers. To address this trend, we believe Congress must review existing statutes, develop legislation where necessary and strengthen enforcement activities. Since last fall, we have spent countless hours trying to develop legislation which would indeed lessen the adverse impact of concentration on agriculture. We have worked very closely with staff members from Sens. Leahy, Daschle and Grassley's offices. We sincerely appreciate your leadership and interest in holding hearings on this issue and are extremely grateful for the untiring efforts of Sens. Daschle, Leahy and Grassley in crafting legislation to address our concerns. Together we learned, and continue to learn, the many and varying complex issues surrounding agriculture concentration and antitrust issues. Together, we attempted to reach attainable, timely solutions. Today, Farm Bureau continues to urge members of this committee to make this issue a priority and to reach a bipartisan solution to address concentration in the agriculture industry this year.

Farm Bureau is very concerned that producers have access to competitive markets. More and more we see producers grow under contractual agreements. As this occurs, we see less importance on traditional cash markets. Since many contracts are based upon cash markets we are concerned that cash markets may become nothing more than salvage markets. This will result in reduced prices for all commodities paid to producers. It is imperative that markets are open to all producers and that these markets offer fair prices for their products.

Many of the concepts proposed by Farm Bureau have been included in either the Daschle/Leahy bill and/or the Grassley bill. Our priorities are for legislation to move this year and for increased involvement in the consolidation issue by the Department of Agriculture (USDA).

Farm Bureau would like to see an expanded role for USDA in evaluating agribusiness mergers and acquisitions which are currently under the jurisdiction of the Department of Justice (DOJ). Broadened USDA responsibility and official consultation with DOJ will ease much of the concern regarding the concentration of agribusiness.

USDA is uniquely positioned and qualified to offer a thorough economic analysis of any proposed merger or acquisition. This is the proper role for USDA. This analysis should be made available to the public and other government agencies.

We are very interested in the model currently being used by the Surface Transportation Board (STB). Under that model, the Department of Justice is required to provide an analysis on proposed mergers and a recommendation on whether to approve a merger to the STB. STB in turn is required to give the Justice Department analysis significant weight in the decision-making process, but is not required to live by the DOJ recommendation. This system could be used in reverse for the USDA-DOJ relationship.

Farm Bureau does not believe the proper role of USDA is to become the enforcement agency, judge or jury in any given antitrust situation. That is the responsibility of the Department of Justice. The USDA analysis should include:

a) the effect the acquisition or merger will have on prices paid to growers due to reduced opportunities to bargain with more buyers;
b) the likelihood that the acquisition or merger will result in significantly increased market power for the new entity;
c) the likelihood that the acquisition or merger will increase the potential for anticompetitive or predatory pricing action; and
d) whether the acquisition or merger will adversely affect producers on a regional basis.

Farm Bureau would like to see the following additional actions considered in the concentration debate:

1. The Grain Inspection, Packers and Stockyards Administration (GIPSA) may need additional resources to investigate anti-competitive pricing practices. Farm Bureau members would like to see better publicizing of these investigations, the results of the findings, and whether civil penalties were imposed. We know that much of this information is confidential and cannot be released. However, we believe GIPSA could provide more information regarding (a) number and types of ongoing investigations; (b) past investigations that resulted in civil penalties being imposed; (c) total amounts of the penalties imposed; and (d) current GIPSA activities that would be beneficial to producers. Further, additional resources are needed in order to properly prosecute offenders. This will help assure a fair system for all producers. We believe a portion of any additional resources secured by GIPSA should be specifically

earmarked for increasing the number of litigating attorneys available to GIPSA to allow it to more comprehensively and effectively pursue enforcement activities.

2. GIPSA should be able to evaluate actions taken by packers who purchase plants and then shut them down. This has the effect of limiting competition in the area and reducing the number of marketing opportunities for independent producers. While GIPSA should balance the capacity needs, environmental considerations and other financial issues of the packers, these actions are contributing to concentration within the meat packing industry. Smithfield's announcement that it would shut down the hog processing lines once it purchased Farmland's Dubuque, Iowa, pork plant is a good example. This action may well result in substantially lower prices for producers of the 7,800 hogs that are processed or slaughtered each day at that plant. A GIPSA analysis prior to these mergers would be valuable to agricultural producers. If the GIPSA analysis shows that a plant closing would have a major impact on producers, then steps could be taken to try to keep the plant open.

3. GIPSA should be allowed to ask for reparations for producers that can show damage as well as civil penalties when a packer is found to be engaged in predatory or unfair practices.

4. Contract poultry growers should be provided the same protections as livestock producers by extending the powers of GIPSA to cover live poultry dealers in the same fashion as packers of cattle and swine are covered. In addition, GIPSA authority should be extended to cover producers of poultry and domestic fowl raised for non-slaughter purposes.

5. Farm Bureau has long supported authorization for a statutory trust for the protection of cash sellers to livestock dealers.

6. More transparency is necessary. It is basic human nature that anyone provided limited information becomes highly skeptical, no matter the circumstances. Farmers become especially skeptical when no information is forthcoming and the result is a constriction of the number of marketing outlets in their local area. The transparency of information regarding mergers, acquisitions and anticompetitive activities must be enhanced.

7. Farm Bureau supports appointing an Assistant Attorney General at DOJ with the sole responsibility of handling agricultural mergers and acquisitions. DOJ has an enormous job these days with consolidations and mergers in so many industries. Counsel specifically focused on agriculture would be able to give the time necessary to make certain that the proposed consolidation would be best for all stakeholders. This position should be created at a level to require Senate confirmation.

8. We support an increase in the staff of the Transportation, Energy and Agriculture section of the DOJ. One way of securing more resources without additional cost to the government would be to increase the current filing fee for each acquiring firm under premerger notification provisions of the Hart, Scott, Rodino (HSR) amendment. Currently under HSR, the DOJ or the Federal Trade Commission must evaluate a merger if one firm has assets or annual sales of $10 million or more, the other has assets or annual sales of $100 million or more and the transaction is valued at more than $15 million. The acquiring party must pay a

filing fee of $45,000. These fees could be increased for larger mergers and then earmarked for additional staff.

9. The enforcement of confidentiality clauses in livestock and grain production contracts should be prohibited except to the extent that a legitimate trade secret is being protected. The objective is to bar the enforcement of confidentiality clauses that seek to prevent dissemination of information about the material terms and conditions of contracts without any legitimate trade secret basis. The primary practical effect of such provisions appears to be to inhibit producers from discussing, comparing and contrasting the differing types of contractual arrangements with their bankers, lawyers and accountants.

10. USDA should be required to assimilate, maintain and disseminate, upon request, detailed information relative to corporate structure, strategic alliances, and joint ventures for all agribusiness entities with annual sale in excess of $100 million.

11. Producers may need government assistance to develop co-ops that will add value to their product and legal structures that will help them to develop relationships with other producers to pool resources and compete in today's economy.

There are several examples of this type of cooperative, which are formed to help farmers optimize profit opportunities for their members. In Illinois, we have Producer's Alliance, an organization with 330 members representing 450,000 acres of farmland. We are dedicated to identifying and developing value-added business opportunities for farmer members.

Pork America is another good example. Recently, a nationwide group of independent pork producers have formed a cooperative that they anticipate will optimize profit opportunities for members. The co-op will assist in coordinating production, processing, distribution and marketing. Pork America plans to operate with limited assets, undertaking activities through partnerships, alliances and other arrangements. It seems a worthwhile venture, but one that will require some initial capitalization aid from the government.

Another boost for cooperatives would be to allow the USDA's Rural Business and Industry Guaranteed Loan Program to make loan guarantees to farmer-owned projects that add value and are built in urban areas exceeding a population of 50,000 people. A group of turkey producers are interested in developing a value-added processing facility in Michigan and are seeking the assistance of the Rural Business and Industry Guaranteed Loan Program. The plant that they wish to acquire is located in a city with a population over the cap of 50,000 people and they are therefore ineligible for assistance. While we certainly want USDA funds targeted to rural areas, this population cap seems too restrictive.

In closing, let me reiterate our desire for a bipartisan effort to address this issue

DOCUMENTS SUBMITTED FOR THE RECORD

April 27, 2000

GORDON H. SMITH
OREGON

COMMITTEES:
BUDGET
ENERGY AND NATURAL RESOURCES
FOREIGN RELATIONS

United States Senate
WASHINGTON, DC 20510-3704

SENATOR GORDON H. SMITH
Statement for the Senate Agriculture Committee
Agriculture Concentration and Competition Hearing
April 27, 2000

Thank you Mr. Chairman and fellow colleagues of the Agriculture Committee for your leadership on behalf of America's farmers and ranchers. I am pleased to have an opportunity to express my views today on the important issue of agribusiness and antitrust matters. As a former food processor, I think I bring a unique perspective to this issue here in the Senate.

As you know, Mr. Chairman, I ran a frozen food processing business in rural Eastern Oregon for many years before being elected to the Senate. After years of practicing law in Arizona, I returned to Oregon in 1980 to try and save the family frozen food business. Despite the fact that there were numerous and much larger competitors in the industry, I was able -- with the help of very capable employees -- to turn around the fortunes of Smith Frozen Foods and return the business to profitability. It is with this experience in mind that I view issues relating to agribusiness here in the United States Senate.

I am well aware that these are difficult times in rural America. Every time I go home to Pendleton, Oregon, I am reminded of the hardships that farmers and ranchers are enduring with low commodity prices. Many of my neighbors in Umatilla County are wheat producers. As you all know, wheat prices -- along with most other program commodity prices -- have seen historic lows in recent years. In addition, there are few bright spots in the picture for the rest of Oregon agriculture -- the specialty crops that range from hazelnuts to potatoes. For example, just last week, onion growers in Malheur County told me that they had to dump thousands of pounds of onions they were storing from last year's crop because there is no market for them. And unlike most of the program commodity producers, our specialty crop farmers have by and large not been the beneficiaries of the billions in assistance that has been distributed by the federal government in recent years.

I want to point out, however, that despite a few notable exceptions, these are not rosy times for food processors either. Food processors operate, as farmers do, in an increasingly competitive and global marketplace in which they are challenged by rising costs of labor, packaging, energy, distribution, and marketing. One need only look at the stock price of virtually any agribusiness to see that these are generally not viewed by investors as high-growth opportunities. There have been a host of recent articles in financial publications about the weak performance of agribusinesses and the need for many food companies to merge in order to remain profitable. Overall, the food processing business continues to be one of very low margins and many companies are forced to seek efficiencies through mergers.

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In addition, large supermarket chains -- also subject to global market trends -- have consolidated and increased their bargaining power with food processors, thereby greatly reducing the ability of food processors to simply increase their prices when the cost of production rises. While all of this has been good news for American consumers who now pay less of their income on food than at any time before, it has meant that the entire food industry has been challenged to capture efficiencies, implement new technology, and cut costs wherever possible.

There is no doubt that global competition is being felt throughout the food business all the way down to the family farm. The question is, what do we do about it? I, for one, do not believe that we can turn back the clock or somehow freeze the forces of globalization in one particular sector of the economy. I am not convinced that this would be a good thing to do even if we could. I believe free markets and open trade are the best way to deliver goods and services to consumers and spread growth and prosperity. I am concerned that we may expend a great deal of effort here in the Senate on trying to defy these forces of change and consolidation, while missing an opportunity to take common-sense steps that will ease this transition for small farmers and ranchers.

The poor conditions in the farm economy have made many of us here in the Senate question federal farm policy and search for ways to help family farmers and ranchers. Many have turned to this issue of antitrust enforcement in agribusiness and the problem of ensuring farmers a variety of buyers for their product while allowing the food industry to innovate and become more competitive. Certainly, we can all agree that it is important that farmers have an opportunity to sell their product in a competitive environment. However, I am unconvinced that there is a need to provide the Department of Agriculture with a new role in antitrust enforcement. In fact, I would be very concerned about the long-term implications to the competitiveness of America's food industry if the Department of Agriculture is allowed to routinely intervene in business practices that are, on the whole, done out of necessity for companies to maintain profitability. It stuns me that we would even consider singling out this industry for such rigorous scrutiny in a way we wouldn't dream of doing to other industries -- such as the technology and entertainment industries. I do not believe we can handicap one facet of the American economy in this manner and not expect it to negatively impact future growth in the industry. Agribusiness and farmers are fundamentally interrelated. The food industry needs to be competitive in order to continue providing an outlet for farmer's products. In the long term, you simply cannot benefit the food producer by hurting the food processor.

As you all know, the Department of Justice and the Federal Trade Commission have held jurisdiction in this area for a long time, and I believe they remain the appropriate agencies to engage in the complicated process of assessing the impacts of proposed mergers. As I pointed out during debate on this subject last fall, the Microsoft case is a prime example of how rigorous the Antitrust Division of the Department of Justice can be in its enforcement of antitrust statutes. I have also cited numerous recent instances in which the Department of Justice blocked mergers or acquisitions in the food industry until major divestitures were completed. Since last year's debate, the DOJ appointed a special counsel in the Antitrust Division that specializes in

agribusiness matters. I think we should give this agency the chance to do an adequate job with the tools it presently has.

What strikes me is that there are a number of ways we can help farmers that are, I believe, much more effective in the long-term than tinkering with antitrust law, yet have not been acted upon. The federal government can do a number of things to reduce the family farmer's cost of production and ultimately increase profitability of their operations. These steps range from tax reform to regulatory relief. I can't tell you how many times family farmers have complained to me about the inheritance tax and how it drives so many family farms out of business. There is no reason why tax reform for farmers should not be amongst our top priorities in agriculture this year.

Another area of concern in my state is the never-ending deluge of new environmental regulations. From expensive measures related to salmon recovery under the Endangered Species Act to new Total Maximum Daily Load policies under the Clean Water Act -- a number of these environmental regulations have a much greater impact on the farmers' bottom line. I have been approached by farmers concerned about the implementation of the Food Quality Protection Act numerous times as well. Perhaps the most worrisome of all of these issues for agriculture producers in my state is the possibility that the federal government will rip out important hydroelectric dams that provide for navigation and irrigation throughout the interior northwest. Comprehensive reform of our nation's farm labor system and the H-2A program is another area that has not been addressed so far by this Congress, yet is a common concern raised by farmers.

There are also ways in which farmers can increase their profits by adding value to their products. The closer farmers can get their products to the end consumer -- for example through farmers' markets -- the more of the retail food dollar they will capture. To do this, they will have to innovate, discover niche markets, and find ways to control labor and packaging expenses while meeting health and safety regulations -- problems that, as I said, agribusinesses grapple with everyday. Perhaps there are ways we can, in a bipartisan manner, assist farmers that are interested in adding value to their crops. Expanding internet access in rural communities, for example, is something that I think we can all agree would be helpful for farmers interested in finding new marketing opportunities.

Again, Mr. Chairman, what we are seeing in the food industry is part of the globalization that we laud and acclaim in almost every other industry. While we are all concerned about the future of family farmers, we should not fundamentally change the antitrust statutes of this country without giving the Department of Justice an opportunity to implement its more rigorous safeguards for agribusiness competition. Let's at least address some of causes of the farm crisis that we know are caused by the federal government before we point the finger at the private sector in a way that may have unforseen consequences for American competitiveness.

Senator Rod Grams

I would like to commend Chairman Lugar and members of the committee today for holding this hearing concerning the problem of agribusiness concentration and its impact on our family farms. Consolidation in the agribusiness community is an undeniable fact – the four largest meatpacking companies have doubled their portion of the markets for beef and pork since 1980, and now possess 80% of the meat market and 54% of the pork market. Producers are understandably nervous about the dwindling number of buyers and suppliers. No one wants to have only a handful of prospective customers for their product.

At the same time, Congress should not respond to these agribusiness mergers in a way that would harm American competitiveness in world markets. If we were to enact blanket prohibitions against consolidation, we will inevitably force out of business firms that are struggling to survive but that could be rejuvenated by the influx of capital and new strategies that mergers could bring. In our rapidly changing economy, Congress should not cavalierly lock American companies into a certain size and market segment while their foreign competitors are free to adapt to the changing demands of the marketplace.

Because of the concerns I have about market concentration, I have endorsed S.1984, the Lugar-Harkin bill, which would create a position within the Antitrust Division of the Department of Justice to enforce U.S. antitrust laws with respect to the food and agricultural sectors. I think we can all agree that the first practical step Congress can take in addressing market concentration is ensuring that DOJ has the resources it needs to enforce existing laws. I hope you will work with the Judiciary Committee to expeditiously consider this bill.

Finally, Congress should not rush to make agribusiness a scapegoat in the farm economy downturn in order to divert attention from the critical needs of producers that Congress must address to help them be competitive in world markets. Regulatory and crop insurance reform, trade opportunities, and tax reform are just a few of the issues that should be on the Senate's agenda this legislative year.

TN

NAM National Association of Manufacturers

Michael Elias Baroody
Senior Vice President
Policy, Communications and Public Affairs

April 27, 2000

The Honorable Richard Lugar
Chairman
Committee on Agriculture, Nutrition and Forestry
United States Senate
328A Russell Senate Office Building
Washington, DC 20510

Dear Mr. Chairman:

On behalf of the 14,000 members of the National Association of Manufacturers – and the 18 million men and women who make things in America – I ask that you include this letter in the record for today's hearing on S. 2552, the Agriculture Competition Enhancement Act; and S. 2411, the Farmers and Ranchers Fair Competition Act of 2000. The NAM strongly opposes enactment of these measures.

As a general matter, the NAM does not take a position on industry-specific legislation. However, both S. 2252 and S. 2411 threaten sound antitrust principles and include other provisions that would set precedents of general concern.

The NAM is most concerned about granting the Secretary of Agriculture (Secretary) authority to review proposed agribusiness mergers and to impose conditions for merger approval. This directly counters the recent recommendation of the International Competition Policy Advisory Committee (ICPAC), which was composed of highly respected antitrust authorities. In its February 28, 2000 report, a majority of ICPAC members recommended removing what sectoral oversight exists and granting antitrust authority exclusively within the Federal Trade Commission and the Antitrust Division of the U.S. Department of Justice. In addition, ICPAC also extolled state attorneys general "to resist using the antitrust laws to pursue noncompetition objectives," which is advice that could just as well apply to congressional consideration on S. 2252 and S. 2411. (ICPAC Report, Feb 28, 2000, p. 153.) For these reasons, the NAM strongly opposes sectoralizing antitrust law by establishing an Office of Special Counsel for Agriculture, as called for in S. 2252

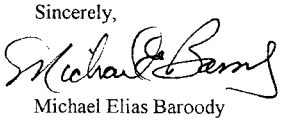
In order to conduct his or her review, S. 2252 would grant the Secretary access to premerger notifications under the Hart-Scott-Rodino (HSR) Amendments to the Clayton Act. The NAM is very concerned about the potential misuse of this highly confidential and proprietary information. While there have never been any leaks by either the Antitrust Division or the Federal Trade Commission, which currently receive the notifications, the potential for such damage would increase by granting additional access.

The sponsors of S. 2411 responded to criticism about granting review of HSR filings by the Secretary of Agriculture by eliminating such access. The current provisions are just as worrisome because the bill would allow the Secretary to promulgate a premerger notification system that is duplicative of premerger filings with the Federal Trade Commission and the Department of Justice.

Another problematic feature of S. 2411 is the establishment of the Family Farmer and Rancher Claims Commission, which would review and award claims to family farmers and ranchers for violations of the legislation. This could set a troublesome precedent for other constituencies. Of utmost concern is that the commission's decisions are subject to judicial review only with respect to the amount of the award. Moreover, the commission would be funded out of fines levied for violating the provisions of Section 4, thus giving the U.S. Department of Agriculture incentive to "find" such violations if the commission needs revenue.

The NAM believes the effects of these bills go far beyond family farmers and ranchers. The prescriptions in S. 2252 and S. 2411 are bad public policy and should be rejected.

Sincerely,



Michael Elias Baroody
Senior Vice President
Policy, Communications and Public Affairs

cc: Members of the Senate Committee on Agriculture, Nutrition and Forestry

PROPOSED RESOLUTION

Passed

RESOLUTION NUMBER: 2000 - N

SUBMITTED BY: Montgomery County Pork Producers Association
Buena Vista County Pork Producers Association
Cherokee County Pork Producers Association
Hancock County Pork Producers Association
Franklin County Pork Producers Association
Dubuque County Pork Producers Association

SUBJECT MATTER: Price Discrimination in Livestock Markets

WHEREAS, The United States Department of Agriculture's Packers and Stockyards Administration has been woefully inadequate in its enforcement of the Packers and Stockyards Act's prohibition of price discrimination and other discriminatory practices by packers; and

WHEREAS, Independent pork producers in Iowa and other states are routinely discriminated against in the market with respect to prices paid for hogs, as demonstrated by USDA's Western Corn Belt Procurement Investigation and other investigations

now therefore be it

RESOLVED, That the Iowa Pork Producers Association and National Pork Producers Council support administrative action or legislation that clarifies the definition of and prohibits price discrimination and reiterates the authority of the Secretary of Agriculture to challenge such discrimination; and

be it further

RESOLVED, That until such federal legislation is passed the Iowa Pork Producers Association and National Pork Producers Council should press for aggressive enforcement of the Packers and Stockyards Act prohibition of discriminatory practices under current authority.

Effective Date if Adopted: Immediate
National – Reaffirms Current Policy

570

PROPOSED RESOLUTION

Passed

RESOLUTION NUMBER: 2000 – L (1)

SUBMITTED BY: Plymouth County Pork Producers Association

SUBJECT MATTER: Packer Ownership of Hogs and Cattle

WHEREAS, Independent livestock producers are efficient and can compete on an even playing field; and

WHEREAS, Packers are creating a trend of vertical integration and creating an unfair advantage; and

WHEREAS, Efficient producers will be forced out of business due to lack of markets

now therefore be it

RESOLVED, The Iowa Pork Producers Association and National Pork Producers Council should encourage and back federal legislation that would ban packers, excluding closed coops, from owning hogs or cattle, directly or indirectly.

Effective Date if Adopted: Immediate
National – Amends Current Policy

570

PROPOSED RESOLUTION

Passed

RESOLUTION NUMBER: 2000 – 10

SUBMITTED BY: Emmet County Pork Producers Association

SUBJECT MATTER: Support House Bills That Ban Packer Ownership of Hogs

WHEREAS, It is very important for our producers to have a competitive market for our product; and

WHEREAS, Packer ownership of hogs is illegal in Iowa yet it is being permitted in other states at this time; and

WHEREAS, Packer ownership of hogs skews the competitive market and price discovery and will also limit the accuracy of mandatory price reporting

now therefore be it

RESOLVED, The Iowa Pork Producers Association fully supports Representative David Minge (D-MN) and a group of ten (10) bipartisan lawmakers introduced on November 10, 1999 to the legislature and in October, 1999 Senator Tim Johnson (D-SD) introduced a bill. Both bills ban packers from owning hogs more than fourteen (14) days prior to slaughter, and both bills call for packers to divest their present holdings and both exempt producer-owned cooperatives.

Effective Date if Adopted: Immediate
State – Amends Current Policy

570

PROPOSED RESOLUTION

passed

RESOLUTION NUMBER: 2000 - I

SUBMITTED BY: Buena Vista County Pork Producers Association
Palo Alto County Pork Producers Association
Montgomery County Pork Producers Association

SUBJECT MATTER: Agribusiness Merger Moratorium

WHEREAS, Rapid concentration in agricultural input companies as well as meat packing and other agricultural processing sectors is reducing competition, destroying markets, and dramatically diminishing opportunities for pork producers in Iowa and beyond; and

WHEREAS, There must be a time of rational reflection on the impacts of agribusiness mergers, a review of relevant antitrust laws, and reform of relevant antitrust laws where necessary

now therefore be it

RESOLVED, That the Iowa Pork Producers Association and National Pork Producers Council support an 18 month moratorium on agricultural mergers involving firms with over $100 million in assets and revenues.

Effective Date if Adopted: Immediate
National – New Topic

510

PROPOSED RESOLUTION

Passed

RESOLUTION NUMBER: 2000 - 5

SUBMITTED BY: Hancock County Pork Producers Association
Dubuque County Pork Producers Association
Franklin County Pork Producers Association
Clayton County Pork Producers Association

SUBJECT MATTER: Country of Origin Labeling

WHEREAS, Consumer confidence is essential for continued growth of domestic pork consumption; and

WHEREAS, Other countries allow use of antibiotics banned in the U.S.

now therefore be it

RESOLVED, The Iowa Pork Producers Association supports country of origin labeling on all pork products sold in the U.S.

Effective Date if Adopted: Immediate
State - Reaffirms Current Policy

220

PROPOSED RESOLUTION

Passed

RESOLUTION NUMBER: 2000 - A

SUBMITTED BY: Kossuth County Pork Producers Association

SUBJECT MATTER: Number of Lean Hog Futures Trading Months

WHEREAS, The Kossuth County Pork Producers and other producers need to be able to market pigs year around; and

WHEREAS, The volume of trading in the Lean Hog Futures on the Chicago Mercantile Exchange has increased significantly; and

WHEREAS, The absence of certain trading months during the year, reduce the producers marketing choices during those months

now therefore be it

RESOLVED, The Iowa Pork Producers Association encourages the National Pork Producers Council and the United States Department of Agriculture to lobby the Chicago Mercantile Exchange to list three (3) additional months (May, September and January) to more effectively serve traders in these transitional months.

Effective Date if Adopted: Immediate
National – New Topic

PROPOSED RESOLUTION

Passed

RESOLUTION NUMBER: 2000 - 2

SUBMITTED BY: Iowa Pork Producers Association Cooperation Task Force

SUBJECT MATTER: Iowa Pork New Generation Cooperative

WHEREAS, Pork producers have received lower profits and price volatility compared to the rest of the pork chain while the structure of the pork industry is moving toward an aligned production system; and

WHEREAS, Iowa Pork Producers Association Cooperation Task Force has completed market research resulting in potential market opportunities for producer owned closed cooperative and the task force has conducted a producer survey which resulted in overwhelming support for a producer owned closed cooperative organization; and

WHEREAS, The Iowa Pork Producers Association Cooperation Task Force has investigated existing producer-owned New Generation Cooperatives and LLC's which many have resulted in added benefit to producers that were previously suffering from limited market access and profitability

now therefore be it

RESOLVED, That the Iowa Pork Producers Association proceed with the development of a producer-owned organization that will include member marketing services; and

be it further

RESOLVED, The organization establish the goal of marketing pork products from the producer owned organization.

Effective Date if Adopted: Immediate
State – New Topic

201

CREDIT SUISSE | FIRST BOSTON

CREDIT SUISSE FIRST BOSTON CORPORATION

Equity Research

Americas | U.S./Food and Agribusiness | March 15, 2000

Presentation to the House and Senate Agriculture Committees

Agribusiness and the Current Economy

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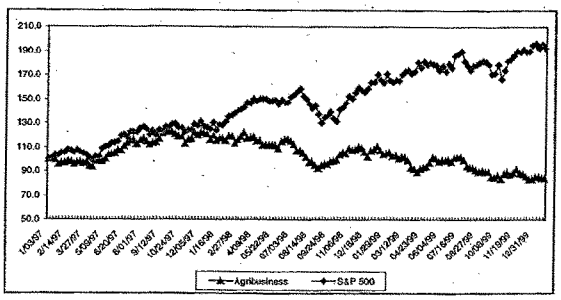


- **Given a number of new proposals that would take agricultural policy in new directions, we were recently asked to share our views on agriculture and agribusiness with the House and Senate Agriculture Committees.**
- **We pointed out that the hardships currently suffered by farmers are being shared by all participants in the food value chain, and are part of an overall power shift taking place upstream toward the consumer.**
- **Agribusiness and food companies still lack the future prospects for which investors are willing to pay: growth, return on capital, and predictability.**
- **We shared our perspectives on the negative impact that proposals for government investment in pork-packing capacity, restrictions on agribusiness mergers, and packer ownership of livestock would have on the sector.**

Agribusiness Stock and Economic Return Review

The current agribusiness environment is challenging. We believe that Agribusiness stocks continue to underperform partly because of the market's narrow focus on technology stocks and the continuation of depressed conditions across many sectors. Following is a review of the earnings and economic returns of the major agribusiness companies.

Archer Daniels Midland (ADM, Hold)

ADM has had little earnings growth and a declining return on invested capital (ROIC) over the past decade. Some of the weakness in recent years has been associated with deterioration in the operating environment owing to weakness in the overall agricultural economy. The magic questions for investors are, what proportion of the poor returns are related to industry trends, how much are poor investment decisions by the company, and how much might be related to a structural decline in the value of some of the company's assets given changes in the economy. If we assume a $17 billion normalized sales base and a 7% operating margin (which was between 8-9% in the early 1990s), we believe normalized EPS might be near $1.40 per share.

Exhibit 1
ADM Earnings Per Share

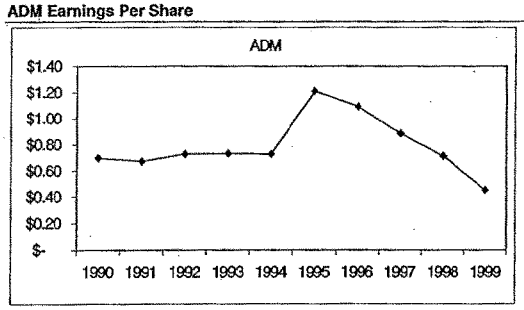


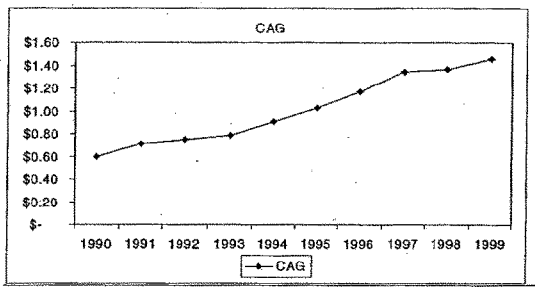
Exhibit 2
ADM ROIC-WACC Breakdown

Year	Economic Profit (MM)	NOPAT (MM)	ROIC	WACC	Invested Capital (MM)
1990	123	595	14.0%	11%	4239
1991	-20	485	10.6%	11%	4589
1992	70	596	11.6%	10%	5362
1993	93	642	11.5%	10%	5794
1994	67	653	10.5%	10%	6654
1995	222	905	12.6%	10%	7668
1996	250	994	12.9%	10%	7808
1997	-475	314	3.8%	9%	8641
1998	-113	613	6.5%	8%	10255
1999	-382	508	5.1%	9%	9785

ConAgra (CAG, Hold)

ConAgra has posted 9% growth, but that's below the company's 14% growth objective, and does not include about $1.3 billion in restructuring charges. Also, keep in mind the rest of the market has done about twice as well. The fact that almost all of this growth has been from packaged foods indicates little expansion in the profitability of agribusiness.

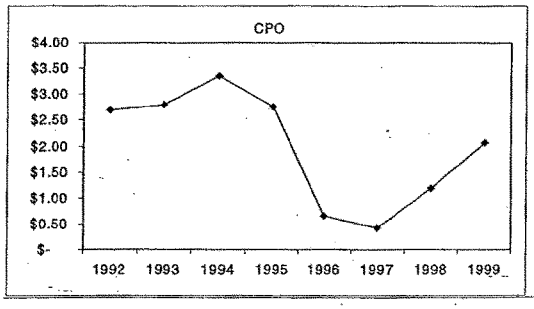
Exhibit 3
CAG Earnings Per Share



Corn Products International (CPO, Hold)

The earnings of CPO, which was formerly a division of CPC international, reflect challenges created when the industry, after an upswing in the mid-1990s, began building new plants (especially the cooperatives).

Exhibit 4
CPO Earnings Per Share



Deere & Co. (DE, Not Followed)

In our opinion, DE's earnings reflect the lack of stability apparent in many agribusiness stocks. Here, we believe the earnings and profit losses mirror the farm

economy and the psychological pinch being felt by farmers, who are consequently unable to make new equipment purchases.

Exhibit 5
DE Earnings Per Share

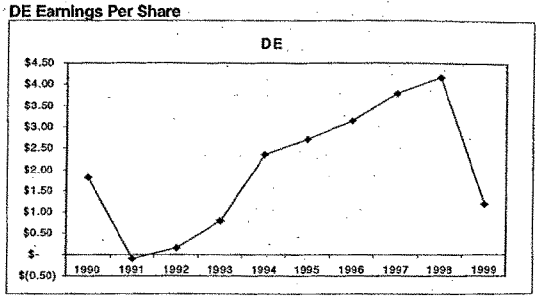


Exhibit 6
DE ROIC-WACC Breakdown

Year	Economic Profit (MM)	NOPAT (MM)	ROIC	WACC	Invested Capital (MM)
1990	-25	542.0	10.4%	10.9%	5204.1
1991	-479	105.1	1.9%	10.8%	5407.4
1992	-418	165.8	3.0%	10.7%	5453.5
1993	-364	269.9	4.5%	10.6%	5977.5
1994	-3	677.3	11.4%	11.4%	5965.9
1995	34	786.6	12.1%	11.6%	6488.7
1996	109	883.9	13.3%	11.7%	6625.7
1997	166	1011.2	14.1%	11.8%	7159.7
1998	130.5	1103.9	13.0%	11.5%	8464.1
1999	-625.2	321.2	3.9%	11.5%	8229.2

Hormel (HRL, Hold)

We are impressed with the improving trend in Hormel's earnings and ROIC (the trend is everything), driven by good new product innovation (such as its "Always Tender" line) and solid execution. Hormel has adopted the EVA® framework for management decision making and compensation over the past year, which may further improve capital allocation decisions. We do note that Hormel's practice of sharing ownership—and profitability—of its hogs with its producers has had a negative impact on earnings, costing them about $65 million (approximately $0.50 per share) in fiscal 1998, and about $100 million in fiscal 1999. The fact that earnings still increased underscores the value of the company's move upstream into more consumer-friendly products such as smoked pork chops and precooked microwaveable bacon.

Exhibit 7
HRL Earnings Per Share

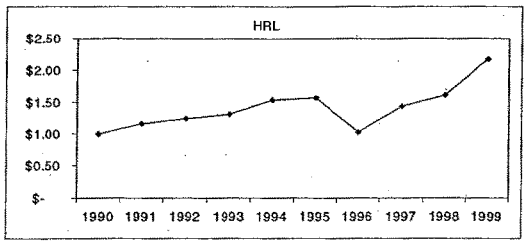


Exhibit 8
HRL ROIC-WACC Breakdown

Year	Economic Profit (MM)	NOPAT (MM)	ROIC	WACC	Invested Capital (MM)
1990	22	96	15.6%	12.1%	612
1991	9	81	13.3%	11.9%	602
1992	10	83	13.9%	12.2%	593
1993	14	94	13.4%	11.7%	809
1994	17	111	13.8%	11.6%	795
1995	26	122	14.1%	11.3%	935
1996	-32	79	7.6%	10.7%	1101
1997	-19	110	9.3%	10.8%	1259
1998	13	125	10.3%	9.2%	1198
1999	45	154	13.0%	9.2%	1168

IBP (IBP, Hold)

IBP's earnings and return on invested capital have been volatile, largely following the ups and downs of its beef packing operations. As the company has been investing heavily to move further upstream into processing, economic returns may well improve. The concern for investors is whether the greater magnitude of returns from processed meats will sufficiently offset prospects for declines in beef and pork-packing margins, which have been quite volatile. These are likely given declines in livestock supplies owing to lower capacity utilization.

Exhibit 9
IBP Earnings Per Share

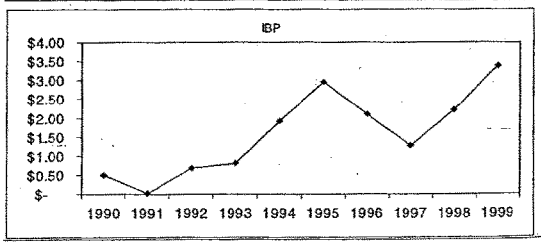


Exhibit 10
IBP ROIC-WACC Breakdown

Year	Economic Profit (MM)	NOPAT (MM)	ROIC	WACC	Invested Capital (MM)
1990	-42	77	6.4%	9.8%	1209
1991	-67	29	3.1%	8.8%	1174
1992	1	111	9.2%	9.2%	1227
1993	-9	108	8.7%	9.4%	1273
1994	70	196	14.9%	9.8%	1360
1995	146	291	20.2%	10.6%	1527
1996	52	217	13.3%	10.3%	1720
1997	-19	158	7.8%	8.6%	2320
1998	24	247	9.4%	8.4%	2470
1999	129	351	14.0%	8.7%	2419

Potash (POT, Not followed)

A quick look at the returns of the Potash Corporation gives us a sense of the challenges in the fertilizer industry, as nitrogen and phosphate prices had a difficult 1999.

Exhibit 11
POT ROIC-WACC Breakdown

Year	Economic Profit (MM)	NOPAT (MM)	ROIC	WACC	Invested Capital (MM)
1990	-63	34	3.8%	10.9%	885
1991	-52	44	5.0%	10.9%	880
1992	-44	50	5.6%	10.6%	879
1993	-42	53	5.6%	10.0%	943
1994	-5	95	9.6%	10.1%	985
1995	46	196	11.7%	8.9%	1675
1996	69	248	10.5%	7.6%	2349
1997	117	363	11.2%	7.6%	3243
1998	41	402	9.6%	8.6%	4194
1999	-604	-357	-9.1%	9.5%	3920

Smithfield Foods (SFD, Buy)

In terms of total shareholder returns, Smithfield Foods has been the best performing dry food company over the past 20 years. Smithfield has an extremely impressive track record of expanding its capital base. Most recently this expansion has taken the form of acquisitions of hog production operations, which we view as opportunistic following the sharp downturn in profitability in that sector. The challenge for Smithfield is to translate these investments into improved profitability.

Exhibit 12
SFD Earnings Per Share

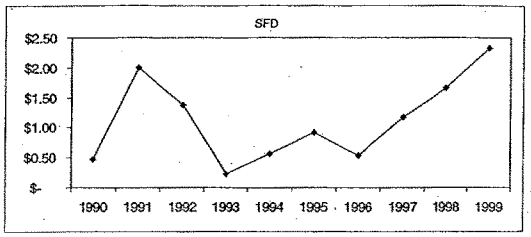


Exhibit 13
SFD ROIC-WACC Breakdown

Year	Economic Profit (MM)	NOPAT (MM)	ROIC	WACC	Invested Capital (MM)
1990	-2	12	8.3%	9.7%	148
1991	16	33	20.2%	11.4%	184
1992	2	24	11.2%	10.5%	253
1993	-21	14	4.4%	10.0%	372
1994	-9	32	8.2%	10.4%	403
1995	2	44	9.6%	9.3%	523
1996	-25	38	6.1%	9.5%	739
1997	-11	67	8.5%	9.8%	844
1998	9	94	9.9%	8.9%	943
1999	27	127	10.0%	8.2%	1491

Tyson Foods (TSN, Buy)

The industry's largest chicken company, with approximately a 34% market share, Tyson had a stellar track record in the 1970s and 1980s. However, the company's investments outside its core chicken operations and changes affecting the chicken industry overall have had a dramatic negative impact on the company's economic profit history in the 1990s. Recently, the company has refocused on chicken and has adopted an EVA® orientation for management that we believe will improve its capital allocation decisions.

Exhibit 14
TSN Earnings Per Share

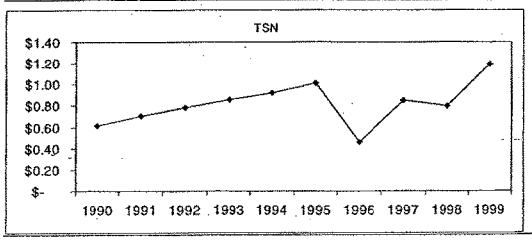
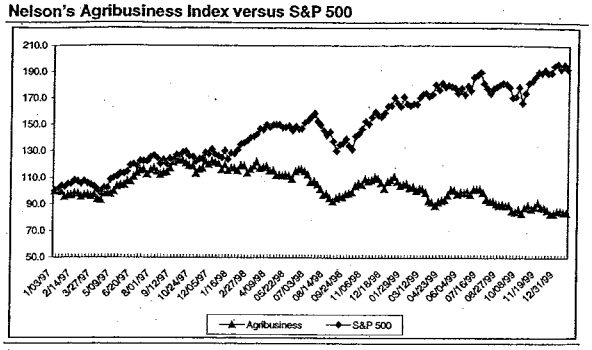


Exhibit 15
TSN ROIC-WACC Breakdown

Year	Economic Profit (MM)	NOPAT (MM)	ROIC	WACC	Invested Capital (MM)
1990	26	231	10.9%	9.7%	2112
1991	-10	204	9.3%	9.7%	2278
1992	20	242	10.6%	9.7%	2316
1993	-5	249	9.5%	9.7%	2921
1994	-61	186	6.0%	7.8%	3322
1995	-1	329	8.9%	8.9%	4065
1996	-168	197	4.8%	8.8%	4183
1997	-111	290	7.1%	9.9%	4002
1998	-187	214	4.8%	8.6%	4919
1999	-47	388	8.0%	9.0%	4760

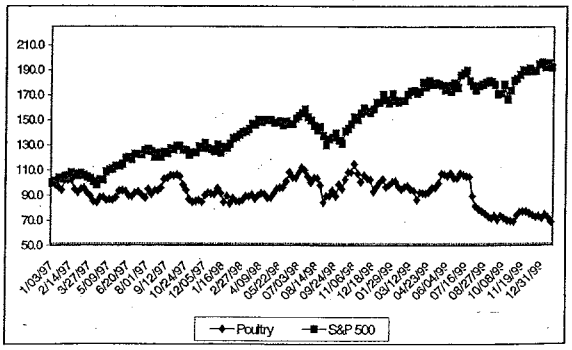
Industry Overviews

Exhibit 16
Nelson's Agribusiness Index versus S&P 500



Chicken Stocks The chicken industry has certainly been the worst-performing group among our indexes in recent years. The industry has had continued problems in supply management, too often striving for volume or share rather than profitability. Investors have been so burned in this segment over the past decade that it may take some time to restore investor confidence. After all, it was just last July when we saw one of the sharpest chicken price declines in our memory.

Exhibit 17
Nelson's Poultry Index versus the S&P 500

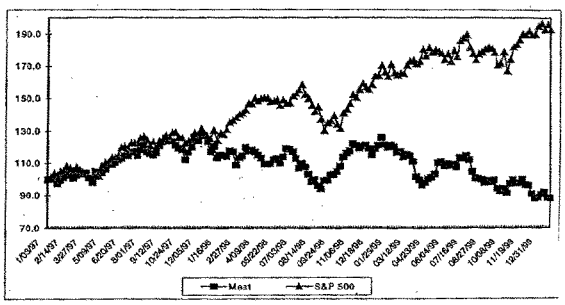


Source: Credit Suisse First Boston.

Meat Stocks Meat companies have also been quite disappointing for investors. Inconsistent returns combined with investor concerns regarding prospective cattle

and hog herd liquidation have turned away investors. Most meat companies are trying to transform their companies in one way or another. As mentioned earlier, Hormel has moved into more consumer-oriented products with its successful line of "Always Tender" products, while the company assures itself of a quality and quantity of supply through contracts with hog farmers. IBP is rapidly moving up the value curve through acquisitions in the processed meat industry, while so far avoiding backward integration. Smithfield has embraced vertical integration and capitalized on opportunities to invest in hog growing operations with last year's downturn in hog prices. All of these efforts demonstrate that these companies recognize the dramatic changes taking place in this industry and reflect an attempt to improve returns that were too often lackluster in the 1990s.

Exhibit 18
Nelson's Meat Index versus S&P 500

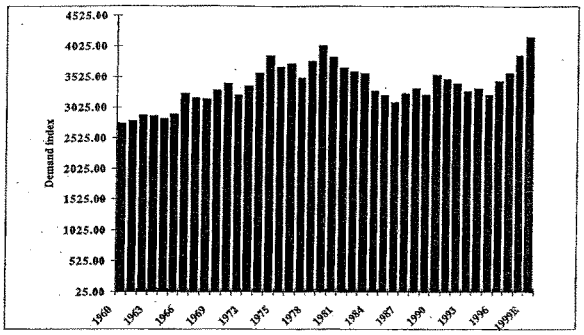


Source: Credit Suisse First Boston.

These index declines occurred despite the fact that we believe demand rose for all major meats last year. We calculate demand for each of these products by multiplying volume produced by average retail price adjusted by the GDP deflator. This method, although simple, incorporates price and volume components, both of which we consider to be important. Such an equation also incorporates some export demand factor, since with other things being equal, domestic prices would tend to rise as supply was diverted to export markets.

Chicken Demand Index Chicken demand rose 11.2%, driven by volume growth of 6.5% and average price improvement of 4.7%. In addition to health, nutrition, and value characteristics, the ability of chicken to absorb flavors, withstand freezing and the microwave, and take on different shapes (malleability) continue to drive demand. We see no end to chicken demand growth in the foreseeable future. The question for investors, however, is one of profitable growth.

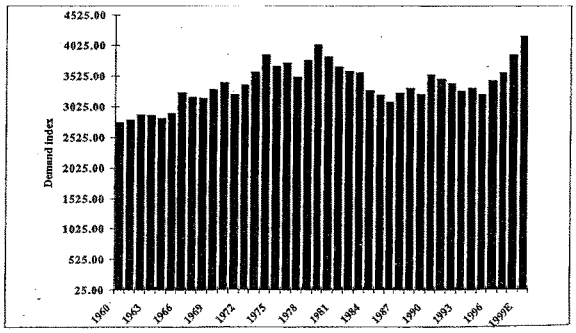
Exhibit 19
Nelson's Chicken Demand Index



Source: Credit Suisse First Boston.

Pork Demand Index Pork demand rose 7.8%, driven by 1.6% volume growth and a 7.4% increase in average retail price. The difference between hog prices of $8 per hundredweight in December 1998 and $38 per hundredweight in December 1999 was consumer demand (without considering the conspiracy theories of some hog producers). Processors are making great strides to make their products more consistent and consumer-friendly, and we note again the success of Hormel's "Always Tender" pork and precooked microwaveable bacon as outstanding examples.

Exhibit 20
Nelson's Pork Demand Index

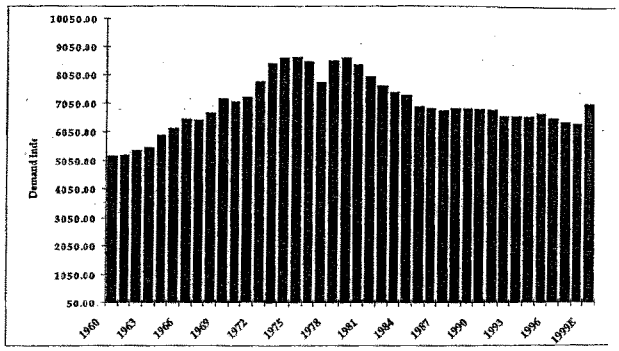


Source: Credit Suisse First Boston.

Beef Demand Index Beef demand rose last year by 10.7%, a substantial increase for the first time in 20 years. Volume rose 2.9% with the peaking of the

supply cycle, with pricing up 7.9%. The industry is doing a modestly better job of product presentation at the retail level (e.g., organizing cuts by cooking method). Demand for steak is great, but product from over half the animal (the chuck and the round) remains a difficult proposition to the consumer.

Exhibit 21
Nelson's Beef Demand Index

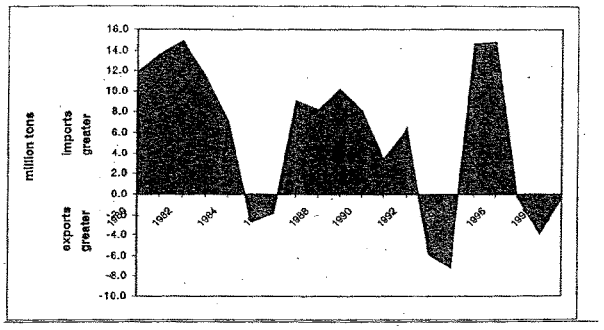


Source: Credit Suisse First Boston.

Why Have Things Been So Bad

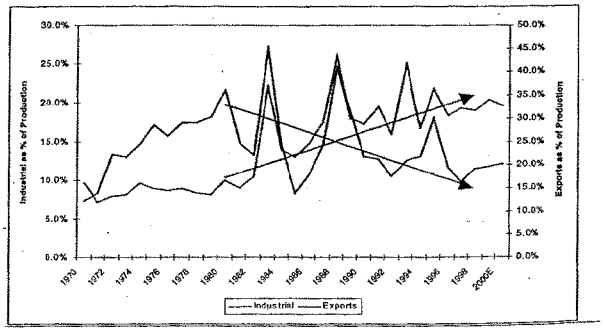
Many factors, both domestic and abroad, are contributing to the challenges currently faced by the agribusiness. One reason is the fact that China has become a net grain exporter versus being a major importer, which it was for much of the last two decades. Given the difficulties already evidenced this year in negotiating more favorable trade terms with China, this condition doesn't look to be changing in the near future.

Exhibit 22
China Net Grain Trade



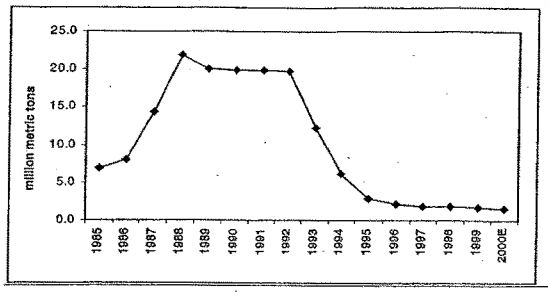
Another source of pressure on agribusiness has been inefficient asset allocation. A prime example can be seen in corn production. Over the past 20 years, the industrial use of corn (ethanol, starch, and fructose) has gone up nicely, while exports have gone down owing to lost markets. The difficulty is that companies that had set up their elevators to where the grain was going, namely exports, are left with assets that are out of place and therefore diminished in value.

Exhibit 23
Industrial Use and Exports as a Percent of U.S. Corn Production



One of these lost export markets has been the Russian grain market, which was strong up until the early 1990s. With imports to the former Soviet Union dropping from a peak of 21.8 million tons in 1988 to 1.7 million in 1999, this market is not likely to return in the near future.

Exhibit 24
Former Soviet Union Grain Imports



Competition from Brazil, which expects this year to contribute another 10 million tons of soybeans and currently enjoys a strong dollar, is also an area that can be expected to affect agribusiness in the United States.

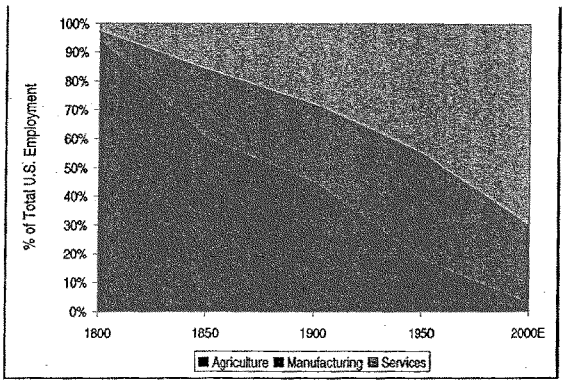
Overall, the conditions in this competitive environment are changing rapidly:

- Increasing pressure from cooperatives, which aren't under the constraints of maximizing earnings and efficiency, has disrupted the profitability margins in the corn and soybean processing industries, as well as the meat industry (Farmland's purchase of inefficient beef processing plants in Dubuque).
- Traditional private firms such as Andre, Bunge, and Continental, have begun searching for a new mission.
- New, nontraditional interveners such as Monsanto, DuPont, and Dow are entering. The level of competition in this arena is exemplified by Pioneer Hi-Bred's story. PHI, a significant player in genetically modified crop (GMO) development, had lower recurring earnings in fiscal 1999 than 1997. This was despite the fact that those were the biggest two years of ramp-up in GMOs, and PHI had no incremental costs (they had paid-up licenses for round-up beans and BT corn). The loss was purely due to competition and the sacrifice of market share.
- Web-based entrants like Rooster.com, E-Markets.com, and emerge.com are pressuring companies to maximize supply-chain efficiency to adapt to new Internet-driven business models.

Things To Consider

You Can't Stem the Flow of History For over 200 years, improving agricultural productivity has allowed a shift in our population from farms to factories and now to higher-value service jobs. Even if we wanted to keep more people on the farm philosophically, we probably don't have enough money in the budget to fight this long-term trend. Europe of course is fighting this, but their constrictive employment policies are costing them a role in the new information-driven global economy. The reality is that we only have about 100,000 real full-time farm operations in the United States anymore that derive their total income from farming. This is a tough business and a tough life. But we have to ask ourselves how much and what type of support is necessary and appropriate.

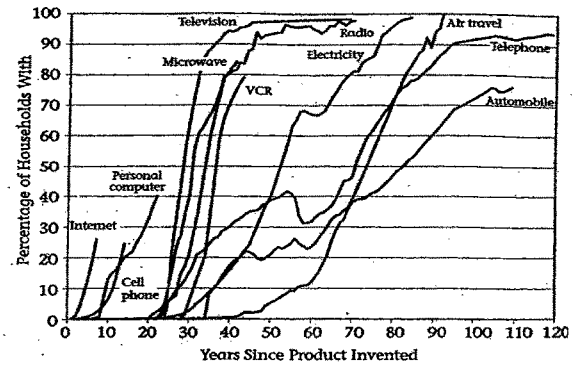
Exhibit 25
The Changing Economy
as a percentage of the domestic workforce



Source: *Myths of Rich and Poor*, by W. Michael Cox and Richard Alm, and CSFB estimates.

The Current Pace of Change Is Accelerating Agribusiness companies are having to run faster and jump higher simply to keep up with the competitive environment. There is little tolerance for poor returns as opportunity costs rise. Rational investors pay for growth, return on capital, and stability—areas in which agribusiness companies have had difficulties delivering. At the same time, the need to invest to keep pace with change is increasing. For instance, farmers adopted genetically modified crops much faster than any of the prognosticators forecasted. The chart on the following page describes how the pace of adoption of new consumer technologies has increased over the years.

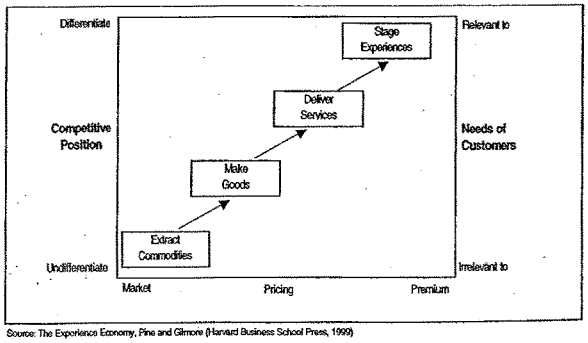
Exhibit 26
Spread of Products into American Households



Source: *Myths of Rich & Poor*, W. Michael Cox and Richard Alm; Basic Books, 1999.

Get Closer to the Consumer Everyone in the food chain needs to be more closely connected with the consumer in order to capture value. An abundant, safe, and low-cost food supply is now a given in our society. Like it or not, it is taken for granted like electricity. More value is now being created higher up Maslow's hierarchy with things that have psychic appeal such as specialty, gourmet, or organic products (or cattlemen converting their spread into a dude ranch for vacationing city folk). We are excited about the disintermediating power of the Internet being able to put small and midsize farmers in more direct contact with the consumer.

Exhibit 27
The Progression of Economic Value



Source: The Experience Economy, Pine and Gilmore (Harvard Business School Press, 1999)

The Level of Concentration in Agribusiness Is Normal and Necessary We seem to get a new study on concentration in agribusiness, particularly on beef packing, about every other month. It feels good to lash out like this, but those who do are scaring away anyone who wants to invest in this industry. More importantly, after all these studies no one has found evidence of collusion. The problem for the beef industry is that demand at the consumer level has been falling for 20 years because it doesn't generate a convenient product. Roughly 60% of the animal is the chuck and the round and people don't stay home on Sunday to cook pot roast for four hours anymore.

Exhibit 28
Concentration of Top-Three Agribusiness Firms

Agribusiness	Top 3 firms % of volume
Beef packing	78%
Pork packing	46%
Chicken processing	45%
Corn processing	69%
Soybean processing	68%

Source: CSFB Estimates; Industry Sources

Now the concentration levels cited above are high compared to the fragmented nature of farming, but not by the standards of other industries.

Exhibit 29
Concentration of Top-Three Livestock and Poultry Producers

Livestock and Poultry Production	Top 3 firms % of volume
Cattle feeding	10%
Pork production	15%
Chicken production	46%

Source: CSFB Estimates; Industry Sources

Importantly and interestingly, they are not dissimilar to concentration levels found among major packaged food categories, the primary customers of agribusiness processors.

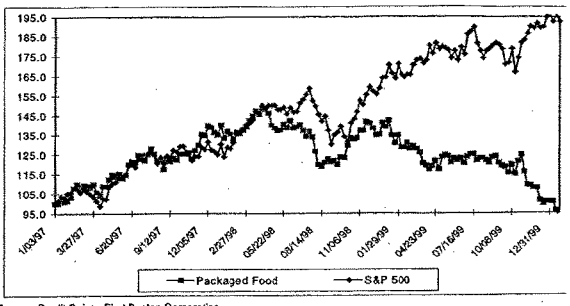
Exhibit 30
Concentration of Top-Three Packaged Food Companies by Category

Packaged Food	Top 3 firms % of volume U.S. retail
RTE cereal	76%
Soup	82%
Frozen dinners/entrees	61%
Cookies/crackers	73%
Confectionery	65%
Ketchup	83%

Source: CSFB Estimates; IRI Data

Let me also highlight that these concentration levels for packaged food companies are not driving growth or predictability either. As noted in the chart below, food stocks are down 20% year to date after declining 24% in 1999 on an absolute basis. Over the last 12 months, food stocks have underperformed the market by about 50%. Before the food retailers are blamed, let me note that food retailing stocks are down about 45%. The entire food value chain is being pressured and compressed. Blaming packers, retailers, or whomever may make some people feel better but won't change the real fundamentals of the situation.

Exhibit 31
Nelson's Packaged Food Index verse the S&P 500



Source: Credit Suisse First Boston Corporation

Current Legislation

Let us close by offering a few comments on some legislative proposals that have surfaced for your consideration regarding their impact on the companies that we follow.

Pork Slaughter Capacity Subsidies New proposals are resurfacing to provide government subsidies to build or lease pork-packing capacity. If the government starts supporting certain processing plants or capacities, it had better be prepared to finance the whole industry. Companies and investors will not invest in expensive new packing plants if they would end up competing against the government, which has infinite resources and even less profit motive than a cooperative. This would set a very dangerous precedent and effectively reduce investment in this area—the opposite of the intention.

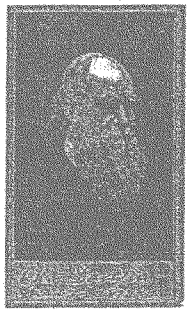
Ban on Packer Ownership of Livestock There are again legislative proposals to restrict and some to ban packer ownership of livestock. First, packers are moving backward in the food production change not because of the romantic appeal of raising pigs. They are doing it to achieve a level of quality and consistency being demanded by the consumer. These investments are expensive, and if they weren't necessary, would probably create a better return upstream in new product development or brand building. In my view, packers aren't doing this because they want to, but because they have to. Second, there are proposals that would not grandfather existing ownership arrangements. Requirements forcing packers to sell off current ownership stakes in production assets would, in our opinion, have a disastrous affect on all livestock production values. There are no buyers for these operations. We believe small and midsize farmers don't have the capital, much less management skills, to buy these operations, and those who want to sell out will see the value of their farms plummet.

Agribusiness Mergers and Acquisition Inhibitions and Moratorium The reality is that agribusinesses are having to consolidate simply to survive. Given the fierce competitive environment outlined earlier, consolidation has become a necessity to execute the cost-cutting needed to survive and to compete against new entrants from places like Brazil and China, and the continuation of highly subsidized competition from Europe. A moratorium on Agribusiness mergers and acquisitions would, in effect, be like shooting the messenger.

Final Thoughts on Agricultural Policy Options

1. Help farmers adapt to the changing economy, rather than further entrench them in nonviable operations. Our economy is based on creative destruction. Farmers and other businesses need to adapt to changes in our economy, or find other ways to make a living. Most nonfarmers now have many jobs throughout their careers and often have to move their families around just to keep up with the curve. Change isn't easy, or even pleasant. But maybe agricultural policy should be more focused on helping farm and rural families to adapt to the new economy rather than trying to preserve them in operations that simply aren't viable.

Exhibit 32
Charles Darwin: "Adapt or Die"



2. Make a conscious decision on the nature and direction of agricultural policy. In our opinion, we need to make a conscious decision regarding what sort of farm policy we want in this country. With the Freedom to Farm Act in 1996, we moved government out of agriculture and planting decisions merely to reinsert government with the bailout packages of the last two years. Do we want a socialist agricultural policy like Europe and render our farmers wards of the state? Maybe we do, given the potential environmental benefits of preserving the countryside. Maybe we don't. But I believe the topic deserves a debate for our country to come to some sort of consensus rather than these one-off packages we've had in recent years.

3. Level the playing field on trade policy. Agricultural trade and production continue to be highly distorted by the large production and export subsidies of the European Union. This is not just costing American farmers, but farmers around the world, in lost markets. In some cases it is preventing farmers in developing countries the ability to step up the first rung on the ladder of economic development. This structural distortion is costing our farmers and taxpayers dearly, in our opinion. We believe that American farmers may never have a viable future until or unless this distortion is addressed.

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Archer Daniels (ADM, Hold, $9.06)
ConAgra (CAG, Hold, $15.53)
Corn Products (CPO, Hold, $22.81)
Deere & Co. (DE, Not Followed, $34.56)
Dow Chemicals (DOW, NA, $97.25)
DuPont (DD, Buy, $47.81)
Hormel (HRL, Hold, $14.13)
IBP (IBP, Hold, $12.81)
Monsanto (MTC, Hold, 41.13)
Potash Corp. (POT, Not Followed, $42.75)
Smithfield Foods (SFD, Buy, $16.44)
Tyson (TSN, Buy, $9.31)

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DEPARTMENT OF AGRICULTURE
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20250

APR 21 2000

The Honorable Albert Gore, Jr., President
United States Senate
The Capitol
Washington, D.C. 20510

Dear Mr. President:

I am transmitting to Congress for its consideration a draft bill, the "U.S. Department of Agriculture Mediation and Arbitration for Agriculture Products in Foreign Commerce Act of 2000," that the Department of Agriculture (USDA) recommends be introduced and enacted.

Sellers of perishable agricultural products, such as fresh fruits and vegetables, encounter numerous obstacles marketing their produce in the course of interstate and foreign commerce. Because of the nature of their products, sellers need to resolve contractual disputes quickly and fairly. In the United States, sellers of fresh fruits and vegetables are protected from unscrupulous business practices under the fair-trading provisions of the Perishable Agricultural Commodities Act (PACA); however, sellers who encounter disputes in international transactions have no such international forum in which to address their problems.

The North American Free Trade Agreement (NAFTA) established the Advisory Committee for Private Commercial Disputes regarding Agricultural Goods to recommend possible systems to resolve these commercial disputes promptly and effectively. On November 20, 1997, the NAFTA Committee on Agricultural Trade recommended establishing a tri-national private dispute resolution system operated and funded by private industry. Following from this recommendation, the produce industries in the three NAFTA countries have formed a tri-national Dispute Resolution Corporation (Corporation), whose mission is resolving commercial disputes between produce companies in Canada, Mexico, and the United States quickly and cost-effectively.

Merchants, the vast majority of which are small businesses, wishing to belong to the Corporation must agree to abide by an established set of trade standards, including the Corporation's use of arbitration or mediation to settle disputes. Firms who refuse to comply with the arbitration or mediation results are "de-listed," or removed from the list of participating firms, an action that will be widely advertised in trade journals and by other means. Prior to entering into a contract, firms can investigate whether a potential contracting partner is "listed" or in good standing with the Corporation and make their decisions accordingly.

The Honorable Albert Gore, Jr., President
Page 2

This legislation amends the Agricultural Marketing Act of 1946 to provide the Secretary of Agriculture authority to accept fees to mediate and arbitrate disputes arising between parties involved in transactions of agricultural products moving in foreign commerce under the jurisdiction of a multi-national entity. This will enable the Agricultural Marketing Service (AMS) to provide contracted mediation and arbitration services to the Corporation, for which it would receive payment.

AMS currently provides similar mediation and arbitration services for fruit and vegetable businesses operating in the United States. Under PACA, AMS resolves more than 2,000 trade disputes each year quickly and inexpensively through mediation and arbitration and an additional 2,200 PACA complaints informally. Because of the training and experience AMS personnel have in Alternative Dispute Resolution, the Corporation has requested AMS to arbitrate its complaints on a user-fee basis.

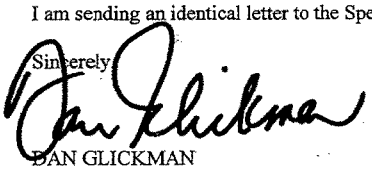
This legislation would make it possible for AMS to provide these services and assist in the development of increased trade in perishable agricultural commodities between Canada, Mexico, and the United States.

The Omnibus Budget Reconciliation Act requires that all revenue and direct spending legislation meet a pay-as-you-go (PAYGO) requirement. That is, no such bill should result in a net budget cost; if it does, it could contribute to a sequester if it is not fully offset. This proposal would affect receipts and, therefore, is subject to the PAYGO requirement. The estimated net budgetary effect of this proposal, however, is zero.

The Office of Management and Budget advises that there is no objection to the presentation of this proposed legislation to Congress from the standpoint of the Administration's program.

I am sending an identical letter to the Speaker of the House.

Sincerely,



DAN GLICKMAN
Secretary

Enclosures

A Bill

To provide the Secretary of Agriculture with the authority to accept fees to mediate and arbitrate disputes arising between parties involved with transactions of agricultural products moving in foreign commerce.

1 *Be it enacted by the Senate and House of Representatives of the United States of America in*
2 *congress assembled,*

3 **SECTION 1. SHORT TITLE**

4 This Act may be cited as the "U. S. Department of Agriculture Mediation and Arbitration for
5 Agriculture Products in Foreign Commerce Act of 2000 ".

6 **SEC. 2.**

7 Section 203 (e) of the Agricultural Marketing Act of 1946 (7 U.S.C. 1622(e)) is amended by
8 inserting before the period the following: ", including the assessment and collection of reasonable fees
9 and late payment penalties to mediate and arbitrate disputes arising between parties in connection with
10 transactions of agricultural products moving in foreign commerce under the jurisdiction of a multi-
11 national entity. Such fees and penalties shall be deposited into the account that incurred the cost of
12 providing such mediation or arbitration services. Any such fees and penalties shall be made available
13 to the Secretary without further appropriation and shall remain available until expended to pay the
14 expenses of the Secretary for providing mediation and arbitration services under this subsection. No
15 person shall be required by the Secretary to use the mediation and arbitration service authorized by this
16 subsection".

REDLINE of the Agricultural Marketing Act of 1946 with Amendments in Bold:

Sec. 203. The Secretary of Agriculture is directed and authorized —

(e) to foster and assist in the development of new or expanded markets (domestic and foreign) and new and expanded uses and in the moving of larger quantities of agricultural products through the private marketing system to consumers in the United States and abroad, **including the assessment and collection of reasonable fees and late payment penalties to mediate and arbitrate disputes arising between parties in connection with transactions of agricultural products moving in foreign commerce under the jurisdiction of a multi-national entity. Such fees and penalties shall be deposited into the account that incurred the cost of providing such mediation or arbitration services. Any such fees and penalties shall be made available to the Secretary without further appropriation and shall remain available until expended to pay the expenses of the Secretary for providing mediation and arbitration services under this subsection. No person shall be required by the Secretary to use the mediation and arbitration service authorized by this subsection.**

CHANGING SUPPLY CHAIN RELATIONSHIPS IN THE LIVESTOCK SECTOR: IMPLICATIONS TO PRODUCERS, RURAL COMMUNITIES AND TO THE LEGISLATIVE AGENDA

Wayne D. Purcell
Alumni Distinguished Professor and
Director, Research Institute on Livestock Pricing
Agricultural and Applied Economics Department
Virginia Tech

Markets are concentrated, old ways of doing business along the supply chain are going away, livestock producers are frustrated, rural communities are changing, and Congress is inclined to try to legislate solutions to economic problems. But in all of this change and upheaval, there is something missing. The facts and the good science are often being ignored.

I want to encourage you to get involved in a more proactive way in this sometimes out-of-control process and make it better for everyone, especially the constituents of the Congressional offices you represent.

There are many people and groups urging that Congress pass laws to regulate the markets and control business behavior in the markets, and all too often, they do not know what they are talking about. Legislation passed on bad information can hurt–perhaps force out of business–the very people and groups that you are trying to help.

I want to encourage all of us to follow the old but wise advice–look before we leap. And in that spirit, I want to deal with some of the assertions, biases, assumptions, and half-truths that are often presented to you as the arguments for legislation. In the process of discussing what is happening, I will develop some thoughts about why we are seeing the growing moves away from the traditional ways of doing things along the production and processing chain between producers and consumers. I hope this approach will help you deal with important challenges that loom in front of all of us.

1. Demand for beef is at record levels but producers are going broke.

This is supposed to convince you that someone in the system is profiteering at the producer's expense. It comes from the president of a state cattlemen's association, a new producer group that is going to court on behalf of producers, a "widely respected" commodity specialist in Chicago--you probably recognize the sources because some of you have heard from them or read their materials.

The facts are that demand for beef decreased every year from 1979 through 1998. This long standing decline in demand is the primary source of the price problems that have put some producers at risk, pushed others out of business, and is a big reason for consolidation in the

processing sector. For beef, it is the catalyst that has forced changes, especially along the producer-packer interface.

Don't assume that this stuff is right just because you hear it over and over or because it is coming from some who should be more responsible than they are in what they say. They treat per capita consumption as an indicator of demand, but per capita consumption is a disappearance number and is a measure of supply, not demand. They look only at price and not the quantity moving through the marketplace, but demand is a price-quantity concept, not price or quantity alone. They have no understanding of the need to adjust price data for price inflation before analyzing what is happening to demand. They do not understand what demand is and is not, and are often totally unqualified to make any such assertions about demand.

This totally wrong stuff about demand has been in the way of those trying to do something about the problem and, without a doubt, has hurt the beef business and everyone in it, including producers. It has decreased the ability of the beef sector to compete for market share, and the overall situation is not much better in pork. It is very important that we recognize and understand that the pressing need to do something about demand is a factor in the moves to contracts and other non-price means of coordination and getting to quality control and toward being truly consumer driven.

Go up to www.aaec.vt.edu/rilp, the web site for the Research Institute on Livestock Pricing (RILP) and look under publications for the **Primer on Beef Demand.** That is a good place to start if you need help in sorting through all the stuff you hear. Look at more sophisticated work on this site **(Measures of Changes in Demand for Beef, Pork and Chicken, 1975-1998),** or go to Kansas State's web site in the Agricultural Economics department, for a very recent study of beef demand. And do not listen to anyone who does not see and understand that decease in beef demand was the most important cause of change in the beef industry across the past 20 years. That influence reached right down to the rural community level as producers have had to consolidate, with some going out of business, in order to get costs down and survive. And it reached the producers in the form of non-price means of coordinating with the needs of the processing sector.

2. The percent of the consumer's food dollar coming to producers is going down and that means controls are needed to keep producers from being exploited.

That trend is not going to change. Producers' get what is left over after middlemen's margins are extracted from what the consuming public will pay. Producers are "price takers" because there are so many of them that no one can influence the market. But the processor and the retailer do not fit that "price taker" model. They will pull out a margin to cover their costs and give some return on investment or they will get out of the business. If their costs--labor, refrigeration, packaging, waste management, complying with new food safety laws--go up, they will pull a bigger margin to cover those increased costs. And unless the retail price is going up rapidly, it is a tautology that the percent of the food dollar coming to the producer will go down over time.

And you know, I trust, that retail prices for beef and pork have not gone up over the past two decades. In inflation-adjusted terms, the continuing problems in demand brought record low prices in the late 1990s. In nominal terms before adjusting for inflation, current retail beef prices are well below levels reached in earlier years.

Again, look at the **Primer on Beef Demand** and the **White Paper on Status, Conflicts, Issues, Opportunities, and Needs in the U.S. Beef Industry**. Unless there are dramatic increases in efficiency and cost-reducing technology at the processing or retailing level, the percent of the food dollar to the producer will continue to come down. The only way to reverse that would be for producers to get involved in more value added processing, but be very careful here. Food processing is a low margin business and producer owned processing operations, especially if they are smaller than the norm in the industry, are typically going to lose money because their costs will be higher.

3. **Processors have moved to non-price means of coordination such as vertical integration, captive supplies, and contracting to control the marketplace at the expense of producers.**

Processors do have some control over their livestock procurement methods. We would be naïve to assume that large for-profit firms are not able to exert some influence over use of contracts and terms of trade. That is what happens in the business world. In most agricultural commodities, the percentage of product grown under contract with a buyer is large and growing.

But when I step back and look at what has happened, another important reason for the integration and contract arrangements we have seen jumps out at me. It is very important that we understand the base level economic reason for the move to contracts and to vertical alliances in the livestock sector, and that understand why this has happened and what it means to producers.

The price-based system in livestock has failed, and failed miserably. Price signals are supposed to move down from the consumer and prompt needed changes at the producing and processing levels. There has been no pricing to value and no recognizable price signals to producers in cattle or hogs, except at the most simplistic of levels.

For price signals to work, we need grades that identify all the product attributes of major importance to consumers. You cannot hook a price signal to a product attribute that is not identified in the pricing process. But we never had grades that identified important value differences in pork or beef. Meat scientists have known for many years that 20 to 25 percent of the Choice grade beefsteaks were too tough to chew. This is an appalling level of product failure that has been an important factor in the 20-year trend of decreases in beef demand, but the obvious shortcoming of the public grades was not fixed. The USDA has a policy that they will adjust grades (they could put in a 1 to 5 tenderness score within the Choice grade, for example) only if the industry demands a change. But that is not going to happen--roughly half of the fed cattle are selling at one price each week and selling for much more than they would be worth if tenderness were added to the grading system. That part of the industry is not going to be interested in changing the grades. (Recall there was a huge unrest in the industry a few years

back when the USDA did respond to an industry initiative and acted to remove most of the B-maturity cattle from the Choice and Select grades).

To keep a price-based system and the rural community with many independent producers, we needed a price system that communicated effectively and an effective market news reporting system so the small producer could be well informed and compete. In the early 1990s, the federal budget for the federal-state market news system was cut hard, and important states like California totally eliminated any financial support.

In a price-based system that did not work, did not provide the quality control so necessary to merchandising programs here and in markets like Japan, we should not be surprised to see the processors move to non-price systems of coordination. And we need to remember that the initiatives are not just at the processing level: in beef, producers are moving aggressively to distance themselves from the failed price system and to organize alliances so they can get rewarded for excellence and value.

4. Prices of cattle are sometimes lower when the level of contracting is higher, and these captive supplies are the reason for the lower prices.

Correlation is not causation. Illegal drug use in the U.S. has increased with increases in ministers' salaries, but we do not naively assume that ministers are now buying more drugs given their better incomes. Extensive research, including research financed by the Congress and administered by Packers and Stockyards, finds no economically important relationship between the level of captive supplies and prices paid for cattle. That research has been ignored by those who do not like the findings, and they continue to argue their cause and look for legislative control.

Go to the RILP web site and look at the publications coming from Kansas State and Oklahoma State Universities. There is added detail on these and other and more recent studies on the Packers and Stockyards web site (www.usda.gov/gipsa/). And there is another side of this issue. Contracting allows even scheduling of cattle and hogs through a processing facility and the RILP site has work directed by James Trapp at Oklahoma State (**Estimated Value of Non-Price Vertical Coordination in the Fed Cattle Market** by John D. Anderson and James N. Trapp) that shows costs of slaughtering and fabricating go up significantly if daily or hourly operating levels are variable. This is especially true when there are not enough animals to reach the optimum per-hour or per-day operating level. To the extent stable and cost-reducing flows have come with contracting, some of that cost-reducing benefit has been bid back into cattle and hog prices that may be higher than they otherwise would have been.

The supply chain is changed significantly in going away from the traditional price-based system. But the price system has not been supported by needed changes in grading in our public grading programs and market news reporting has not kept up in the race for control. The price-based marketplace is losing the race, and we are now often concerned about a competitive base price in some of the contracts and formula buying arrangements.

This is a complex area, deserving of much more thoughtful consideration than to assign causation based on the fact that two or more things are correlated in that they are occurring at the same time. We have already seen that moving to contracts and buying arrangements was arguably a necessary move to get the quality control needed to develop modern and consumer-driven merchandising programs. And there is no body of research that supports the often-made claim that the use of contracts is pushing producer prices down.

5. Contracts and formula price arrangements are changing the price discovery process and that is why producers' prices in recent years have been low.

Price discovery is changing, and there are issues with which we should be concerned. I do not like the situation that we see in public grades and grading, and I do not like the cuts in the budgets for economic planning information and market news. And I certainly do not like selling many of the market-ready fed cattle in a 2-hour time window each week with essentially all the cattle going at the same average price. That is not effective price discovery, and I hope we see it change -- hope we get to pricing individual animals on a carcass basis, and get there soon. More hogs are sold on a carcass basis, but there are still issues in comparing bids and the often-complex pricing grids being used.

But there is a difference between price discovery and price determination. Prices are eventually determined by the interaction of supply and demand and a market-clearing price will be determined by supply and demand. Price discovery is the dynamic process of looking for that market-clearing price. If beef demand is weak and declining, fed cattle supplies are increasing, and average slaughter weights are approaching or are at record high levels (the situation throughout 1998), the marketplace will discover a lower price. It has to, or the added tonnage would never get moved through the pipelines.

Don't blame the low prices during this type of period on price discovery--the culprits are weak demand and/or heavy supplies. The marketplace must and will find and "determine" a lower price in this set of circumstances, no matter what the price discovery mechanisms might be.

The "white paper" on the RILP website (referenced above) has an excellent discussion of price discovery and price determination and how they are different, written by Clement Ward at Oklahoma State University. It is well worth reading, and I recommend it to you. It is important that we not blame low prices brought on by weak demand and/or a surge in supplies on the price discovery system and try to correct the price problems by controlling how product is bought and sold. That may or may not help keep producers viable as we work through a series of changes and adjustments.

6. Middlemen are taking larger spreads or margins, forcing prices down to producers.

Middlemen's spreads will increase as their costs go up with price inflation. This is a tautology. The only reasons their spreads will not increase is if they give up economic functions to others or adopt cost-reducing technology to eliminate the need to extract a bigger margin to cover inflating costs.

Society would like to see evidence of progressiveness, evidence of effort to innovate and keep costs down. We all would, because reducing costs at the processing level protects the producer against the pressure for lower prices when consumer-level demand decreases. And performance here has not been bad as we watch the livestock marketplace change.

If you adjust beef packers' spreads for inflation, those spreads have trended down since the early 1980s. In spite of the fact that they are now doing more trimming and packaging (added responsibilities will increase spreads in most of food processing), they have not had to increase their spreads of margins in lock step with overall price inflation. The spreads for pork packers, when adjusted for inflation, also move slightly lower.

We would always like to see even better performance, but the packing sector has been progressive in adopting cost-reducing technology. They have thus been able to constrain that downward pressure on producers' prices that would come from margins expanding with fully inflated input costs--and still report out good profits.

Andy Gottschalk, a widely quoted industry analyst, has estimated beef packers' per-head weekly profit margins for many years. The average for the decade of the 1990s is about $5 per head, with many weeks and a few entire years averaging negative margins. Even $10 per head is about 10 percent of the hide and byproduct credit for slaughter cattle. Packers fabricate and offer boxes of beef without taking anything more than a small portion of the non-meat credits. As you will hear from the industry analysts, this is a low margin business with the low costs coming from high-volume operations essential to profitable business results.

You can find analysis of the spreads in the RILP publication **Sources of Better Prices for Cattle Producers** on the RILP website. As you will find in that publication, it is the retailer's margin that has tended to increase with price inflation across recent years. Expanding retail margins do put pressure on producers' prices, but it is hard to adopt a posture that the retailers should not be allowed to expand margins to cover inflating costs. We would hope for innovation and cost-reducing technology, but there is less evidence of that at the retailer level than at the processor level.

SOME OVERALL THOUGHTS

There are other presumptions, assumptions, and emotions that get presented as fact, but this list should suffice to support the need for you to be informed, to know what the facts are. And you will need to keep in mind that when the research is consulted, it may get used in a selective way if you are still hearing from an advocacy group.

Last week, we saw widespread publication of a claim that captive supplies have cost cattle producers a billion dollars. It is interesting how this number was generated.

In a mid-1990s study, Packers and Stockyards looked at a large number of cattle transactions in Texas. They reported analysis that indicated a 1 percent increase in captive supplies was

associated with an $.08 per hundredweight decrease in fed cattle prices. This result was generally consistent with the findings in the earlier Packers and Stockyards administered studies with Kansas State and Oklahoma State doing the work. That earlier work found a small negative impact (less than $1 per head on a $700 to $800 animal) for some forms of captive supplies (and a small and less than $1 per head positive impact for some other forms). But this is the first time any of these results have been misused as they appear to have been in the recent releases.

A Nebraska group took the $.08 and multiplied it by 42 since, the group said, captive supplies have been at the 42 percent level. The $.08 impact is at the margin, the impact of the last 1 percent change in captive supplies. It is inappropriate to multiply that coefficient by 42 and thereby assume that the same result would hold over a huge range of 1 to 42 percent in captive supplies. But that is in fact what was done, resulting in a presumed impact of some $3.42 per hundredweight, or $40 per head. If you extend that across all the 25 million or so cattle that are slaughtered in a year, the result is $1 billion.

No objective researcher would misuse a research finding in this way, but there is nothing objective about this reporting. It is from an advocacy group that has been championing the need to control the way packers buy cattle and to outlaw most types of contract buying. The research was consulted, but not in an objective way.

The supply chain in livestock is changing. It means change for producers as they are asked to change how they do business and how they value and sell their livestock. We all had a liking for the old price system and the institutions it supported at the local level, but that system is being replaced. Had we been wise enough to nurture, support, and change the price system as needs changed and the consumer reclaimed the right to be served, it might have been continued. But it is the year 2000 and there will be little patience with a system that still does not price to value, still does not identify and price attributes of importance to consumers, still does not guarantee even a modicum of quality control, and continues to try to value livestock on a live basis where guessing at true value is inevitable and totally unreliable.

But as change continues, we have a constituency that does not want to see change, does not see it as appropriate. That constituency correctly understands that change will extend to producers and to our rural communities, and that change is not wanted or welcomed. To stop the changes to a non-price system of coordination, there is a tendency to call for legislation to stop the change and restore what once was.

Someone needs to intervene in this process, because much of the advocated legislative agenda is based on assumption, bias, and innuendo. Before all the "misinformation" is wrapped into a package of support for legislation and marketplace regulation, it is important that you be in a position to sort fact from fiction and avoid the obvious traps. Ask some hard questions, because the future of the producing community is at risk here and what we do will be very important.

Ask:

What is the source of better prices for producers from a more regulated marketplace? Where is the added money to come from?

If a regular flow of slaughter livestock through the processing facilities really does, as the research shows, reduce processing costs, is it possible that producers' prices would go down and not up if contract buying were eliminated?

As independent producers have a harder job trying to fit into integrated and contract controlled livestock sectors, would it have been this way if grades had been modernized and market news budgets increased instead of being cut? Is there anything that can be done--even at this late date?

Who is going to cover the added costs associated with the mandatory price reporting? Will it be producers?

Where is the use of the objective research, from the researchers that do not have an axe to grind and who want the entire business to prosper to help producers, processors and consumers? Who do you turn to?

For nearly 15 years, the Research Institute on Livestock Pricing has been conducting research at Virginia Tech and helping finance work at other land grant universities to provide a solid base of information on which to make policy and market regulation decisions. Why is it that I have never heard from any of you as you look, I would hope, for objective information on which to base your advice and to use in drafting proposed legislation?

There is a gap here, a missing link that I hope we can work together and fill. I believe all of your constituents, and especially those who contact you from our rural communities, would be the beneficiaries. The consolidation and change along the supply chain is a predictable and expected response to a failed pricing system for cattle and hogs. It has changed the current operating environment and the future outlook for your producer constituents. But as a public, we stood aside and watched the price-based livestock economy start to die. There is less room for the independent thinking entrepreneur in the non-price systems we are seeing evolve. But when the price system failed, these non-price systems are the path to the coordination and quality control essential to the modern global marketplace. Keeping the rural community intact and characterized by a number of entrepreneurial farm families may be, perhaps surely is, a worthy policy goal in this country and is one worthy of our discussion, dialogue, and debate. But that discussion and dialogue is not happening in the livestock sector. What we are seeing is a well-intended (I hope and trust) attempt to protect that atomistic structure in our rural communities by controlling and regulating the marketplace into which those producers sell. And I have major concerns that this indirect approach may end up hurting those same rural communities and the families in them.

And as you reflect on these observations, I would encourage you to step back and think about how successful we have been in this country when we try to legislate solutions to economic problems.

Let's all see if we can find ways to use the legislative process that encourage an efficient and progressive livestock industry that is serving the needs of all involved, including consumers and those rural communities we envision, better and better over time. And I do not believe we will get there with a philosophy that focuses only on regulating the marketplace and fails to see the economic forces that are demanding change and adjustment.

STATEMENT OF NATIONAL MEAT ASSOCIATION REGARDING AGRICULTURAL CONCENTRATION AND COMPETITION

National Meat Association represents packers of all sizes: small, medium, and large. A particularly significant segment of NMA's membership is composed of smaller and medium-sized family owned packers whose very existence and livelihood is threatened by increasing concentration in the meat industry. Because of the concerns of these members, National Meat Association opposes S. 2252 and S. 2411.

S. 2252 would place antitrust enforcement authority outside the Department of Justice, creating a politically charged antitrust process. The proposal would give USDA the ability to oppose the pre-merger review opinions of the Department of Justice, thus pitting one federal agency against another.

S. 2411 would place every packer who purchases livestock at the risk of double jeopardy from damage claims which could be filed with both the Secretary and with a Court. This legislation would also require all businesses that process agricultural commodities, as well as those which do business with the Agriculture sector, annually to disclose highly confidential information about contractual relationships and business alliances.

S. 2252 and S. 2411 fail to address what NMA believes is the primary cause of concentration in the meat packing industry, government intervention and regulation. In addition these measures would impose additional burdens on small and medium-sized meat packers, thereby accelerating concentration in this industry.

The government program which provides what is probably the single largest incentive for increased concentration in the meat industry is the estate tax, which breaks up family-owned firms at least once every generation. While it is an extraordinary event when the government seeks to break up an AT&T or a Microsoft, the government routinely imposes death taxes on family-owned packing firms and family-owned farms which drive them to sell out to their larger corporate competitors.

The proposed legislation would regulate and sometimes prohibit the transactions between companies which provide the liquidity and capital to pay estate taxes. The likely effect of this prohibition would be to drive down the value of these enterprises and force them into bankruptcy. Government mandated illiquidity is unlikely to be an incentive for prosperity and growth among NMA's small and medium-sized packer members. The largest and most successful companies in the meat packing business cannot be held to blame for the inevitable consequences of these federal tax policies.

Another very current example of government policies which increase concentration is the recently enacted mandatory price reporting legislation. When Congress incorporated substantive requirements for mandatory price reporting into the FY 2000 Agricultural Appropriations legislation, it acceded to the demands of the largest packers to require mandatory disclosure, not only from the largest packers, but also from 30-40 small and medium-sized packers who altogether account for only 15-18% of beef slaughter. If the mandatory price reporting data from all of these companies results in a market which is so truly "transparent" as to help smaller producers understand the details of the largest packers businesses, it will unfortunately also be so transparent as to allow the largest packers to identify and overwhelm the niche markets which sustain small and medium-sized packers. We believe this result is not criminal, but that it is inevitable and that the effect of this sweeping new government program will be exactly the opposite of the stated intentions of its sponsors. To avoid this effect, a small and medium-sized packer exemption should be established.

Another example of the regulatory burdens on small and medium-sized meat packers is an inspection system that is more oriented to prosecutions and recalls than to prevention and public health. USDA insists on end product testing for pathogenic bacteria, rather than giving priority to the testing of incoming animals and ingredients. National Meat Association and its members do not oppose testing, but they do oppose testing which is done at a point that is unrelated to the packer's ability to control the tested hazard. End product testing is less effective than prevention-oriented testing of animals and ingredients. Because end product testing is statistically unsound, it puts every packer, large, small, or medium, at a Russian-roulette risk of closure or recall. For a small or medium-sized company, these risks threaten the company's ability to continue in business. Thus, the orientation of FSIS testing to prosecution, rather than prevention, is an additional incentive to leave the meat packing business and invest the family assets in the stock market. This risk is not hypothetical. The highly publicized Hudson ground beef recall resulted in the sale and division of that company's assets among the largest poultry processor and the largest red meat processor. When the government later brought criminal charges against two Hudson executives for withholding information which would have expedited a recall, the individuals were acquitted, after it was shown that the government itself had the information and, because of policies which put prosecution ahead of prevention, had not shared that information with the company or the public.

The appropriate response to increasing concentration in the meat packing business is to fairly monitor and identify the causes of concentration, rather than enacting new layers of regulation which will accelerate it. In October 1998, NMA asked Agriculture Secretary Glickman to:

> "Direct the Grain Inspection, Packers & Stockyards Administration (GIPSA), to conduct a continuing monitoring and evaluation of industry concentration and in the unwanted event that firms do go

> out of business, to evaluate whether the manner in which regulations were implemented and enforced is a cause."

In February 1999, the Secretary responded to NMA's request for a Concentration Watch program by pointing out:

> "Concentration in all sectors of agriculture into fewer and fewer hands has long been a concern of mine, and enforcement of the Packers and Stockyards Act (Act) will continue to be a high priority of the Department of Agriculture (USDA)... One aspect of GIPSA's program includes tracking packing firms that cease business in order to determine any impact on industry competition as well as to determine whether there are unpaid sellers of livestock."

While Secretary Glickman did not accept the NMA proposal for a Concentration Watch the idea still has merit. The Congress should ask the General Accounting Office to contact the executives of packing firms which have been sold or closed to determine the extent to which existing government programs or other factors have contributed to concentration.

Finally, NMA urges this committee not adopt legislation which penalizes people for being successful, whether they are small, medium, or large. It is NMA's view that the proposed legislation would create additional burdens for small and medium-sized packers and provide an additional incentive for these firms to leave the packing business, thereby increasing concentration. For this reason, enactment of this legislation would be a disservice to producers who would have fewer purchasers for their livestock, to packers, and to ultimate consumers who would have fewer sources from which to purchase meat.

Concentration is a matter of serious concern for NMA. It is time to identify the causes and to not be shy about asking whether government polices have been a major, indeed perhaps the primary cause. If that is the case, Congress is ideally situated to enact remedial legislation.

For further information, please contact Jeremy Russell at 510/763-1533.

Testimony of Merlyn Carlson

Director, Nebraska Department of Agriculture

On the issue of Agriculture Concentration of Ownership and Competitiveness

Senate Agriculture, Nutrition & Forestry Hearing
April 27, 2000

Thank you for allowing me to submit this written testimony regarding the issue of concentration in agriculture. I don't think there is any doubt that mergers and the growing concentration in the agriculture industry are a concern to the producers on farms and ranches in Nebraska and across the United States. More and more, you'll find references to the Cargill/Continental, Pioneer/DuPont, and Smithfield/Murphy Farms mergers mixed into the normal coffee shop talk about the weather and commodity prices.

But the concern about consolidation and mergers is not new, with our current antitrust laws dating back to the late 1800s and early 1900s. I think the difference between then and now is that historically the consolidation has been on only one side of the farm equation. Now, in addition to the mergers of grocery manufacturers and retailers, producers are faced with consolidation of agriculture input suppliers and commodity markets. It's a chain that has seed companies consolidating with chemical companies, and chemical companies consolidating with grain elevators, with the potential to squeeze Rural America in the middle.

I applaud the members of Congress for recognizing this problem and taking the initiative to address the matter through new legislation. It is reassuring to know that the problems in rural America are not going unnoticed, but being met with action.

That said, I offer three points of my own for your consideration in the debate on concentration.

First, I believe that before we can begin to effect appropriate regulations in regard to the structure of the agriculture industry, **we need a thorough and deliberate review of the effectiveness of current anti-trust law and the Packers and Stockyards Act as they apply to the agricultural sector**. Such a study could research whether concentration in agriculture should be regulated differently than other industries.

Second, I believe Congress **needs to provide USDA the financial support necessary to enforce the Packers and Stockyards regulations currently in place and those that may be created in the future**.

Third, I think we need to recognize that agriculture consolidation is not a foreboding, but a reality. This is the path that the marketplace has led us down, and I feel our **best option for battling that trend will be enabling producers to add value back into their raw agriculture products through value-added and cooperative initiatives**.

Effectiveness Study

I have heard arguments both for and against an "Agrarian Antitrust" – laws that would regulate concentration in agriculture separately from the laws established in the Clayton and Sherman Acts long ago. Frankly, I'm not sure on which side of the fence I fall. But as we begin

to debate legislation concerning our current antitrust laws and Packers and Stockyards regulations, I recommend we study the effectiveness of those laws and rules. We need a sound, factual background from which to build the policies that will regulate agriculture in this new century.

This is not a new suggestion, but rather an echo of ideas presented by various groups and individuals, including a state of Nebraska task force and a USDA advisory committee.

In the 1999 legislative session, the Nebraska Unicameral created the Agricultural Structure Assessment Task Force. The group, which was charged with studying the overall structure of agriculture, also was asked to recommend "state and federal legislation which will help to achieve a balance among various types of agricultural entities and, thus, serve the best interests of all the people of the state and nation."

The Task Force was comprised of a mix of producers, agribusiness representatives, educators, and legislators. It conducted what I consider to be a very thorough study, visiting with a number of individuals well-versed in agriculture structure issues. I have enclosed copies of the report for your review.

As part of its analysis, the Task Force reviewed a 1996 report issued by the USDA Advisory Committee on Agricultural Concentration. The Task Force, in its final report, said it supported the findings of the Advisory Committee and suggested to the federal government that the report "deserves more attention than it has received thus far."

Based on that report, I, and the Nebraska Task Force, feel Section 202 of the Packers and Stockyards Act and the current antitrust laws need to be scrutinized and interpreted. Section 202 reads: "it shall be unlawful for any packer with respect to livestock, meats, meat food products, or livestock products in unmanufactured form, or for any live poultry dealer with respect to live poultry to: make or give any undue or unreasonable preference or advantage to any particular person or locality in any respect whatsoever, or subject any particular person or locality to any undue or unreasonable prejudice or disadvantage in any respect whatsoever."

Among the questions the Task Force asked: "Under what conditions would the Departments of Agriculture and Justice take action under current law? Are there specific thresholds? Should there be specific thresholds?"

As far as antitrust law goes, there is no standard trigger for merger violations. Douglas Ross, special counsel for agriculture with the Antitrust Division of the Department of Justice, told folks at the USDA Agricultural Outlook Forum 2000 that there is no "automatic threshold of market concentration that will always result in a determination that a merger would violate" the Clayton Act. My question is whether there should be, or could reasonably be, such a threshold. A study such as the one I am suggesting could look into this issue.

Enforce Current Regulations

Also in the USDA Advisory Committee report, it was suggested the current law, particularly Section 202 of the Packers and Stockyards Act, be enforced. It's a lament I have heard over and over from producers, as well.

I and the Nebraska Task Force agree that enforcement of the Packers and Stockyards Act, as well as the antitrust laws followed by the Department of Justice, would go a long way in protecting farmers and ranchers from unfair market practices. It's a step that needs to be taken, even as the study I recommended above is being conducted. But, financial support is needed.

USDA officials tell me that it's not necessarily lack of desire that's causing a problem in reference to Packers and Stockyards Act enforcement, but rather lack of sufficient finances to

support a solid employee base for that enforcement. The agricultural marketplace has grown. It only makes sense that the number of employees charged with enforcing the regulations imposed upon that marketplace grow in step.

This viewpoint is supported in another USDA study, this one by the National Commission on Small Farms. That group, in January 1998, said in its report that "enforcement of the Packers and Stockyards Act is essential to a healthy market structure for livestock" and urged the Secretary of Agriculture to request increased funding for securing staff necessary to conduct investigations of anti-competitive behavior. It suggests the need for increased economic, statistic, and legal expertise for that purpose.

The Department of Justice has taken an initial step in this direction. In January of this year, DOJ created a new position, Special Counsel on Agriculture, and legislation has been introduced that would keep that position a permanent part of DOJ. I support the legislation, and urge the Special Counsel on Agriculture to work heartily to enforce existing antitrust laws.

The Future in Value-Added

While the ideas I have mentioned above will assist the federal government in its battle against agriculture's market-mongers, I would also like to advocate putting some power back into the hands of producers. The area that I feel holds the best and most immediate opportunity for us to help rural America is the value-added concept.

It's a growing agricultural buzzword that I'm sure many of you are familiar with. It came to the forefront in Nebraska in 1999, when Governor Mike Johanns announced the implementation of a state Value-Added Initiative. He charged the Departments of Agriculture and Economic Development to work together to facilitate a program that would enable producers to add value to their raw agricultural commodities, thus capturing more of the consumer's food dollar.

The initiative has sparked the study of numerous potential projects in the state, and just last month the state Legislature approved $1 million in funding for the next three years to encourage value-added initiatives and entrepreneurial proposals.

I believe it is crucial for the federal government to work in conjunction with states in developing this value-added concept, and other cooperative efforts, to their full potential. While programs that offer financial assistance already are available, more is needed. Also, and maybe just as important, we need improved communication from the federal government on the availability of such financial and technical assistance.

Again, my feelings on this are supported by the National Commission on Small Farms. In its report it calls for, among many things, the promotion of available USDA funding sources to finance feasibility studies and the need for easy access to sound financial, legal, and marketing support for new cooperative ventures.

By readily providing producers with financial, informational, and technical support on value-added and cooperative concepts, we help them help themselves. They develop a sense of ownership that no longer ends at the sale barn floor or elevator scale, and hopefully see an increase in the amount of money in their pockets, rather than the pockets of huge, multi-national corporations.

Final Thoughts

I am certainly not implying that the bills currently before you concerning concentration are a detriment to agriculture. Some of these bills do in fact address issues raised by the USDA

Advisory Committee, the USDA National Commission on Small Farms, and the Nebraska Agricultural Structure Assessment Task Force.

But, I believe that with a study of the effectiveness of concentration law in hand, greater enforcement efforts, and promotion of value-added and cooperative concepts, we can carry our industry into and through the 21st century.

These are not things that rural America can do on its own. We need state-to-federal partnerships and the cooperation of the United States Congress.

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American Cotton Shippers Association

April 26, 2000

Hon. Richard G. Lugar
Chairman, Committee on Agriculture,
Nutrition & Forestry
SR 328A
Washington, DC 20510

Re: Agriculture Concentration & Competition Legislation, S. 2252 & S. 2411

Dear Chairman Lugar:

The American Cotton Shippers Association (ACSA) is unalterably opposed to the inclusion of cotton in pending legislation, S. 2252 , *The Agriculture Competition Enhancement Act*, and S. 2411, *The Farmers and Ranchers Fair Competition Act of 2000*.

Interest of ACSA

ACSA was founded in 1924 and is composed of primary buyers, mill service agents, merchants, shippers, and exporters of raw cotton who are members of four federated associations located in sixteen states throughout the cotton belt:

Atlantic Cotton Association (AL, FL, GA, NC, SC, & VA)
Southern Cotton Association (AR, LA, MS, MO, & TN)
Texas Cotton Association (OK & TX)
Western Cotton Shippers Association (AZ, CA, & NM)

ACSA member firms handle over 80% of the U.S. cotton sold in domestic and export markets. In 1999-2000, domestic mills will consume 10.5 million bales and 7 million bales will be shipped to foreign mills. Because of their involvement in the purchase, sale and shipment of cotton, ACSA members are directly impacted by any action of the Congress that would burden or impede their commercial viability to provide a competitive market price for their producer and textile mill customers in the domestic and export markets.

Proposed Legislation Restricts Competitive Marketing of Cotton

At the heart of each measure is a section [S. 2252 - 5(a)(2) & S. 2411 - 4(a)(2)] which will result in USDA regulation of cotton purchases and sales by making it unlawful for any dealer, processor, commission merchant, or broker *to make or give any undue or unreasonable preference or advantage to any particular person or locality or subject any particular person or locality to any undue or unreasonable disadvantage in connection with any transaction involving any agricultural commodity.*

The concerns over market concentration in sectors of the livestock industry will have the effect of regulating cotton sales and threatens a marketing structure, which over the years has provided cotton producers with an active and competitive market for the sale of cotton.

Sections 4(a)(2) & 5(a)(2) will preclude the offering of price premiums to areas of the cotton belt that produce high quality fiber with strong market demand and the establishment of discounts for poor fiber qualities in other areas. In instances of a short world supply of poorer quality fibers this could result in a premium for the lower qualities, given its world demand, over that of finer qualities produced in that or other regions of the United States. Would such market circumstances be subject to the review of USDA?

Further, this unnecessary and restrictive language precludes discounts for cotton produced and stored in areas where warehouse service is poor and delays are frequently encountered and prohibits the payment of premiums in areas where the warehouses provide timely or even immediate shipment.

This provision would also create havoc with forward contracts entered into with producers from the same region at different points in time at different fixed prices or prices determined by futures market prices. Those who contract at different times or fix the futures price in different months could be deemed to have "an unreasonable preference or advantage." The same is true for those who sell in the spot market at different points in time. All of these situations establish prices and the last thing our industry needs is a USDA bureau determining that marketing factors "subject any particular person or locality to any undue or unreasonable prejudice or disadvantage."

We also have concerns with the restrictions on the sale or acquisition of relatively small merchant businesses, warehouses, and cotton gins with annual net sales of more than $10 million, which is equivalent to handling approximately 25,000 bales of cotton.

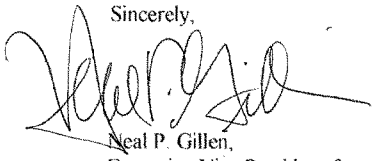
No Compelling Need & No Demand For Regulation of Cotton Industry

This draconian reaction to the current state of the US and world farm economies resulting in large part from adverse economic conditions will do nothing more than worsen the situation. In our view there is no real or government fabricated substitute for competition.

The cotton marketing system is a proven success and a competitive model well suited for the US cotton industry. In no other sector of the farm economy is the factor of competition more prevalent than in the cotton industry. There is no justification for its regulation and the producer segment of our industry has not expressed a desire that cotton be subjected to the provisions of S. 2252 or S. 2411. Therefore, we respectfully request that the Committee exempt cotton and the other price supported commodities from inclusion in the proposed legislation.

We respectfully request that this letter be included in the record of the April 27, 2000 hearings.

Sincerely,



Neal P. Gillen,
Executive Vice President &
General Counsel

JERRY JEROME, *Chairman*
NICK WEAVER, *Vice Chairman &*
Secretary-Treasurer
STUART E. PROCTOR, JR., *President*

Statement of Ted Seger, Farbest Foods

on behalf of the

National Turkey Federation

To the Senate Agriculture Committee

Hearing on Agriculture Concentration and Competition

April 27, 2000

SUITE 400 • 1225 NEW YORK AVENUE, NW • WASHINGTON, DC 20005 • TEL: (202)898-0100 • FAX: (202)898-0203

My name is Ted Seger, and I am the president of Farbest Foods Inc. of Huntingburg, Indiana. Farbest is the nation's 15th-largest turkey processor, producing more than 150 million pounds of turkey meat annually. In addition, my family owns and operates Wabash Valley Produce, a turkey production operation, whose farms produce approximately 400,000 turkeys annually.

I am submitting this statement today on behalf of the National Turkey Federation (NTF), which represents Farbest Foods, my family's turkey growing operations and virtually all U.S. turkey processors, growers, breeders, hatchery owners and allied industry companies. NTF is the only national trade association representing the turkey industry exclusively.

NTF is opposed to S. 2252 and S. 2411 because it believes the legislation creates new antitrust authorities that are unnecessary and that ultimately will do immeasurable harm to the very family farmers it is designed to protect. **To NTF's opposition, I would like to add Farbest Food's strong opposition to both S. 2252 and S. 2411. If either of these bills had been in effect in 1998, they would have been directly responsible for putting hundreds of family farmers who raise turkeys in southern Indiana in jeopardy of losing their turkey operations.** I'd like to take a moment to tell you why.

S. 2252 and S. 2411 are based on the assumption that agribusiness mergers and acquisitions are a prime cause of low prices to family farmers around the country. The bill's authors and cosponsors believe big processors are absorbing or merging with smaller processors at a rate that drastically reduces the number of processing outlets to which family farmers can sell their products, be they grains, row crops or livestock and poultry. The proponents of these bills believe the resulting concentration creates less competition, and thus lower prices, for agriculture products.

What the authors of S. 2252 and S. 2411 apparently have failed to consider is that a merger or acquisition often represents the only option by which a family farmer can preserve the processing outlet to which he or she sells their products. This bill creates so many regulatory barriers to discourage mergers and acquisitions that it is certain to prevent mergers and acquisitions that preserve viable market outlets, boost farm prices and preserve family farms. Farbest's story illustrates exactly how a merger or acquisition can benefit family farmers.

The mid-1990s were financially devastating to the turkey industry. The cost of feed to turkey producers jumped 44 percent in 1996 and remained at a 15-year high through most of 1997. The total cost of turkey production increased 20 percent during this period. At the same time production costs were skyrocketing, industry overproduction and the collapse of some critical export markets led to a 5-percent decrease in the price of whole turkeys and a 9-percent drop in the price of breast meat, our most valuable product. The industry experienced 30 consecutive months of losses; by the first quarter of 1998, Farbest and other turkey processors were losing an average of 11 cents per pound on every turkey we produced.

With processor losses like these, the prices paid to the family farmers who raise turkeys for Farbest and other processors also were declining. In addition, processors were forced to pay less for eggs and poults, and we were buying less from the thousands of men and women who work for allied companies that serve the turkey industry. The processors and family farmers on the front lines of the turkey industry were suffering the worst, but the misery rapidly was spreading to all segments of our industry.

Farbest Foods is not a large processor, and it could not survive indefinitely in such an unprofitable environment. Our losses were staggering, running into the millions of dollars in

both 1996 and 1997. By early 1998, Farbest had only two options available: we could find a partner to merge with or acquire our operation, or we could drastically reduce our operations and sever our contracts with hundreds of family farmers who raise turkeys for us. It was not out of the question that Farbest would have to cease operations entirely. Had that happened, most of the family farmers who raise turkeys for us would have had to cease operations, too. Yes, competing turkey processors may have given contracts to a handful of those growers, but most of the growers simply would have discontinued turkey production as processing capacity in southern Indiana would have been cut in half.

Fortunately for Farbest and for the growers with whom we work, we found that partner. In the summer of 1998, we were able to reach an agreement in which Boar's Head Provision Co., a Brooklyn-based further processor of quality meat and poultry products, acquired many of Farbest's assets. Farbest now is operated as joint venture of Wabash Valley Produce, a production company, and Boar's Head, a further processor.

The results, both for Farbest and for the family farmers who work with us, have been tremendous. With Boar's Head purchasing many of our products, including the valuable breast meat, Farbest is better able to guarantee markets for all its products. The result has been stronger prices, a return to profitability and – most importantly – fair, favorable contracts with the growers who raise turkeys for us. Certainly, the general improvement in the turkey industry has helped, but Farbest's financial situation was so dire that we would not have been in a position without the Boar's Head alliance to take advantage of that industry wide recovery.

Farbest Foods exists today as a strong, vibrant company only because we were able to reach an agreement with Boar's Head. Had the regulatory framework envisioned by S. 2252 and

S. 2411 been in place in 1998, it might have been too costly and too time-consuming to complete the acquisition. Yes, I'm confident USDA and the Justice Department ultimately would have approved the acquisition but I think there is a very real chance that Farbest – and the family farmers who work with us – would have gone under waiting for that approval to occur.

The financial issues facing family farmers and agribusinesses today are complex, and the supporters of S. 2252 and S. 2411 appear to be taking a very simplistic view of the causes of and solutions to those issues. The problem with simplistic solutions is that they often have unintended consequences. For Farbest Foods and a lot of family farmers in southern Indiana, those unintended consequences would have been disastrous.

Thank you for the opportunity to submit this statement.

STATEMENT OF

NATIONAL FARMERS ORGANIZATION

2505 ELWOOD DRIVE

AMES, IA 50010

515-292-2000

SENATE COMMITTEE ON AGRICULTURE,
NUTRITION AND FORESTRY

PRESENTED BY

EUGENE PAUL

April 26, 2000

Statement of Eugene Paul
On behalf of the National Farmers Organization
2505 Elwood Drive
Ames, Iowa 50010

Introduction

The National Farmers Organization represents independent producers nationwide in negotiating contracts and other terms of trade for grain, livestock and dairy. We are in the marketplace doing so on a daily basis. The specific purpose is to help independent producers extract the dollars they need to cashflow their operations, pay their expenses and earn a living from what they produce and sell.

We define an independent producer as one who, with his or her family, resides on their farm, provides day to day management, decision making, controls the marketing of the production, whose capital is at risk, and owns or wants to own that business.

Our basic premise is that an agriculture consisting of independent producers is not only desirable, but essential for maintaining our nations' food production, rural businesses and communities as well as infrastructure.

The most critical component to survival of independent producers is the price received for commodities produced. Prices determined in markets that are open, fair and competitive are essential. A fair price for commodities at the farm gate, due to increased levels of market concentration in most commodity markets, has not been forthcoming and must be addressed. This must be a high priority for all producers. Therefore NFO stands in strong support of S 2411 and S2252.

NFO has felt for some time that a more rigorous enforcement of our anti-trust laws has been needed.

Our members have passed resolutions which support:

Legislation that promotes markets that are open, fair and competitive for owners and operators in family farming.

Any legislative effort that would restrict anti-competitive mergers and acquisitions.

The 20 livestock producing states attorneys' general recommendation to the USDA, including the following: Greater public disclosure of key market information, such as prices paid by packers for fed cattle and slaughter hogs acquired under formula or contract; USDA's close examination of mergers and consolidations in the livestock industry to find if competition will be reduced in violation of the Packers and Stockyards Act or other laws; and, producers should

Today, as many people are focusing on agriculture as they try to determine what is causing the crisis, we need to recognize the importance of the marketing system.

The traditional economic model used to analyze agriculture is the purely competitive model. The model characteristics include: many buyers and sellers, diffused market power and no control over price. Some of these characteristics fit the farm side of the equation, but certainly not the markets farmers sell into. The traditional model allows for producer access to markets that are open, competitive and fair.

Farmers are asking some serious questions about what is open, competitive and fair. What is the correct price and who determines the price? The National Farmers Organization's experience in the markets has found few instances where, when people or entities have the ability to dictate terms of trade including prices, that they don't take full advantage of the opportunity to do so.

As NFO markets livestock and grain for our members, our negotiators feel the impact of the concentration and mergers among buyers.

Concentration in agribusiness is at its highest levels in the 20th century. The Smithfield Foods-Murphy Family Farms merger and Cargill-Continental are just two examples of the concentration of economic power and market signal distortion taking place in agriculture. Concentration levels for the four or five largest firms is at 83% for the four largest beef packers, 57% for hog slaughter, 59% for grain port facilities, and 80% for soybean crushing.

The result of this consolidation means that in many areas there may be two or three processing facilities, but all owned by the same company.

Our basic premise is that an agriculture consisting of independent producers is essential for maintaining our nations' food production, rural businesses, communities and infrastructure.

It is the position of the National Farmers Organization that farmers cannot and should not expect solutions to the current problems in agriculture to come solely from government or government programs. In order to maintain their independence, producers will need to take responsibility for their marketing decisions. They will need to use networking, group marketing and Capper-Volstead bargaining to extract the dollars they need to cashflow their operations, pay the bills and provide for their families.

The independent producer structure of agriculture has served the United States well in providing adequate supplies of wholesome food for our population since our nations' founding. The successful track record of a widely dispersed agriculture dominated by independent producers should not be risked based on

the current short-term track record trend towards consolidation and integration.

Independent producers can remain economically viable only if they have access to markets that are open, fair and competitive. We concur with the Small Farm Commission that the price received for the product produced is the single most critical component for the survival and profitability of independent producers into the 21st Century.

QUESTIONS AND ANSWERS

April 27, 2000

QUESTIONS SUBMITTED BY SENATOR PAT ROBERTS TO MR. JAMES F. RILL

Q. *In your testimony, you state that the International Competition Policy Advisory Committee found that multiple merger reviews impose significant costs on industry participants. If the USDA should become involved in multi jurisdictional reviews, could these significant costs be expected? Could they potentially adversely affect the nation's farmers?*

A. As I indicated in my written testimony, a majority of the member of the International Competition Policy Advisory Committee, or ICPAC, recommended removing the oversight authority for competition-related aspects of merger review from the sectoral agencies and vesting such authority exclusively in the federal antitrust agencies. This recommendation was based on the Committee's concerns regarding the duplication and inefficiency inherent in dual agency merger review. Multiple review of the competitive aspects of mergers imposes significant costs on industry participants because they must address the competition-related aspects of a particular transaction before two or more federal agencies. Dual enforcement creates increased uncertainty regarding review standards and time frames since the process may well differ between agencies. There is every reason to believe that, if the USDA is vested with the authority to review the competition-related aspects of mergers, industry participants will suffer these increased costs of merger review, ansing particularly from uncertainty as to standards.

The proposed legislation imposes legal standards for agribusiness merger review that are far different from, and vague compared to, the well-defined antitrust standards applied by the antitrust enforcement agencies since the early 1900's. For example, S. 2552 (Senator Grassley's bill) would create a special counsel within the USDA for competition matters to review proposed mergers and determine whether they would "cause substantial harm to the ability of independent producers and family farmers to compete in the marketplace." If the merger meets this standard, the special counsel would have power to challenge the proposed merger in court. Under S. 2411 (Senator Daschle's bill), the Secretary of Agriculture would be charged with determining whether a proposed merger could lead to any one of a laundry list of unfair practices, or whether the merger "could be significantly detrimental to the present or future viability of family farms or ranches or rural communities." If these standards are met, the Secretary may then mandate changes to the proposed merger, such as the divestiture of certain assets. If the merging companies fail to adhere to the Secretary's proposed changes, they may be assessed civil penalties.

The standards under both bills are wholly inconsistent with the standards applied by the DOJ. Under Section 7 of the Clayton Act, enacted in 1914, the ultimate question is whether the proposed merger may tend to substantially lessen competition. To make this determination, the antitrust enforcement agencies analyze the future competitive effects of a proposed merger, with particular reference to whether the merger is likely to create or enhance market power or facilitate its exercise to the detriment of consumer welfare. This standard includes full consideration of the effect of a proposed agribusiness merger on family farmers and

suppliers.[1]

The antitrust enforcement agencies have jointly developed the Horizontal Merger Guidelines to describe the detailed, fact-intensive inquiry they will follow to analyze competitive effects.[2] The standards in the proposed bills simply do not require this critical competitive analysis, but are ambiguous and depart from the consumer welfare principle. Consider, for example, that under Senator Daschle's bill, the Secretary can mandate major divestitures of assets if the proposed merger could cause an agricultural dealer "to make any false or misleading statement in connection with any transaction involving any agricultural commodity that is purchased or received in interstate or foreign commerce."

The second part of the question is whether the significant increased costs imposed on industry participants by multiple agency review could potentially adversely affect the nations' farmers. The answer is three-fold. First, increased costs of multiple agency review will be imposed on the parties to the proposed merger, as well as other industry participants, including dealers, processors, brokers, farm and ranch groups, and individual farmers and ranchers, who may well be tasked by multiple agencies to provide voluminous data, documents and testimony regarding the industry and products at issue in a proposed merger. Second, farmers, like all consumers, will be adversely impacted by the higher costs of multiple merger review to the extent that such reviews result in higher tax burdens. Third and most important, to the extent that multi-agency review and restrictive non-competition based standards discourage or prevent mergers that are lawful under the Clayton Act, consumers and society in general will be deprived of the efficiencies that result from pro competitive transactions.

Q. *Could you please elaborate on some of the concerns recently expressed by FCC Commissioners Michael Powell and Harold Furchtgott-Roth regarding dual jurisdiction? In your opinion, could much of these same problems be expected should the USDA be given a large role in merger review?*

A. FCC Commissioners Michael Powell and Harold Furchtgott-Roth have publicly expressed concerns regarding the dual responsibility for review of competitive issues by the FCC and the DOJ Antitrust Division. For example, in recent testimony regarding the Telecommunications Merger Act of 2000, Commissioner Powell testified that the FCC's "comprehensive merger analysis" of telecommunications mergers is "largely duplicative" of the antitrust agencies' competitive evaluation. He underscored that "[t]his imposes significant costs on a transaction. The costs to the parties include greater uncertainty of result, increased legal costs to defend a proposed transaction before multiple agencies, and greater uncertainty of time before closure. The government bears a cost as well with the duplicative expenditure of resources inherent in concurrent jurisdiction. In the FCC's case, scarce resources are diverted from other critical activities." [3]Commissioner Powell added that

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[1] For example, the DOJ concluded from its investigation of the Cargill/Continental Grain merger, that the lessening of competition resulting from the merger would likely have led to farmers receiving less money for their crops that they would have absent the merger. U.S. v. Cargill and Continental Grain, No. 99-1875 (D.D.C. July 8, 1999).

[2] U.S. Dept. of Justice & Federal Trade Comm., Horizontal Merger Guidelines (1992).

[3] Prepared Statement of the Honorable Michael K. Powell, Before the U.S. House of Representatives Subcommittee on Telecommunications, Trade, and Consumer Protection, at 2 (Mar. 14, 2000).

he believes there is room to preserve a role in merger review for the FCC that is complementary or supplementary to that of the antitrust agencies. "The Commission should be constrained to consider only issues such as whether the merger would violate an express provision of the Communications Act or the Commissions' rules. In addition, it is appropriate for it to consider the merger's impact on other communications polices such as media diversity and universal service that are not appropriately considered by antitrust authorities."[4]

Similarly, in his March 14, 2000 testimony on the Telecommunications Merger Act of 2000, Commissioner Furchtgott-Roth testified that the FCC's merger review duplicates that of the DOJ and the FTC, "Merging companies should not have to jump through excessive federal antitrust hoops, and those hoops should be held out by the institutions with the express statutory authority and expertise to do so. Those agencies are the Department of Justice and the FTC. When the FCC gets into the game as well, it increases the costs of the merging parties and expends taxpayer funds, while adding little value from an antitrust perspective." [5]

These is no doubt that the concerns and costs regarding multi-agency merger review, expressed by Commissioners Powell and Furchtgott-Roth, will be realized should the USDA be charged with reviewing the competitive aspects of proposed agribusiness mergers.

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[4] *Id.*

[5] House of Representatives Prepared Statement of the Honorable Harold Furchtgott-Roth, Before the U.S. Subcommittee on Telecommunications, Trade, and Consumer Protection, at 2 (Mar. 14, 2000).