November 19, 2010

J. Dudley Butler, Administrator
Grain Inspection, Packers and Stockyards Administration
United States Department of Agriculture
1400 Independence Avenue SW, Room 1643-S
Washington, DC 20250-3604

RE: Comments on Implementation of Regulations Required Under Title IX of the Food, Conservation and Energy Act of 2008

Dear Administrator Butler:

Thank you for this opportunity to comment on the rule proposed by the Grain Inspection, Packers and Stockyards Administration (GIPSA) under the authority existing within the Packers and Stockyards Act of 1921 (P&S Act). For nearly 15 year the Center for Rural Affairs has called upon the Secretary of Agriculture and the United States Department of Agriculture (USDA) to promulgate rules that allow for more effective and more aggressive enforcement of the Packers and Stockyards Act, especially Section 202(b) of the Act. We are pleased to see this step finally taken and hopeful about the impact on family farmers and ranchers as well as small cities and towns across rural America.

In 1997, the National Commission on Small Farms issued a call for a number of the livestock market reforms that are included in this proposed rule. Chuck Hassebrook, the Executive Director of the Center for Rural Affairs was named by Secretary Dan Glickman as a member of the National Commission on Small Farms and we vociferously supported the livestock market reforms called for in the final report of the Commission, entitled "A Time to Act."

Two years later, the Center for Rural Affairs independently petitioned Secretary Glickman to utilize his existing authority under the Packers and Stockyards Act to write a rule that would provide a definition for what constitutes an "undue or unreasonable preference" as prohibited by the Packers and Stockyards Act, Section 202(b). Secretary Glickman declined to act on our petition.

Since that time the Center for Rural Affairs has remained one of the most outspoken voices on the need for defining an "undue or unreasonable preference" under the Packers and Stockyards Act. During both the 2002 and 2008 Farm Bill debates the Center for Rural Affairs called for the inclusion of a livestock market competition title that included a provision compelling the Secretary of Agriculture to write rules defining and "undue or unreasonable preference" under the Packers and Stockyards Act. In 2008 those efforts were rewarded when just such a provision was included in the Food, Conservation and Energy Act of 2008 (2008 Farm Bill).

The current rule proposed by GIPSA and Secretary Vilsack is a direct result of that provision. In fact, the proposed rule encompasses both section 1105 and section 1106 of the 2008 Farm Bill and includes a definition for "undue and unreasonable preference" along with several other

provisions also called for in the 2008 Farm Bill that seek to address concerns raised by family farmers and ranchers across the country about certain practices in sheep, cattle, hog and poultry markets.

The proposed rule is issued in accordance with Title XI of the 2008 Farm Bill and the authorities granted to the Secretary of Agriculture and the USDA under the P&S Act. The result of this rulemaking process is an historic reform that will greatly benefit family farmers and ranchers for years to come. The Center for Rural Affairs supports the finalization and implementation of this proposed rule. We offer the following comments to assist in improving the proposed rule and in preparation for final implementation.

Undue and Unreasonable Preference

The Packers and Stockyards Act specifically prohibits price discrimination by meatpackers against smaller volume, family farm and ranch livestock producers. Specifically, Section 202(a) of the P&S Act prohibits "*an unfair, unjustly discriminatory, or deceptive practice.*" Section 202(b) of the Act makes it unlawful for packers to "*make or give any undue or unreasonable preference of advantage to any particular person or locality in any respect whatsoever.*"

For example, meatpackers routinely pay five or six cents more per pound, more in some cases, in purely volume-based premiums to the largest hog producers simply because they are large. Six cents may not sound like much of a discount but, for an independent family farmer with 150 sows in a farrow-to-finish operation, it amounts to $56,000* less annually for marketing hogs of the same quality, simply because they markets fewer hogs [**150 sows, 3,600 butcher hogs marketed annually at an average live weight of 260 lbs., and 936,000 lbs. total resulting in an annual discount of $56,160]*.

That is precisely the kind of price discrimination that this rule needs to put an end to. That's what the Center for Rural Affairs set out to accomplish when we worked so diligently to urge Congress to include the "unreasonable preference" rulemaking provision in the 2008 Farm Bill. Independent producers have had increasing market risk and foisted on them as increasing vertical integration and captive supplies have turned them into residual suppliers receiving discriminatory prices for their livestock.

USDA's draft rule is not perfect. But it is the most aggressive livestock market reform to come out of Washington since the passage of the Packers and Stockyards Act itself. It is a strong rule. It should be strengthened, not weakened, and implemented post-haste.

To strengthen the rule, USDA should first do the following – revise the rule to simply, clearly and unequivocally, disallow purely volume-based premiums. Opponents of USDA's GIPSA rule speak often about "value-based marketing." But, despite the current practices and behaviors by large meatpacking corporation, "value-based" is not the same thing as "volume-based," and GIPSA would do well to make that point as clearly as possible.

Moreover, the sections of the proposed rules regarding what constitutes and "unreasonable preference" under the Act focus excessively on treatment of large-volume livestock producers in relation to "groups of producers" at the expense of individual, smaller-volume producers.

Lastly, the proposed rule should be revised to exclude premiums that are based on nebulous, so-called "operational efficiencies" that packers claim occur within the confines of the packing plant itself versus real and verifiable differences in transactional costs related to procuring and handling livestock outside the plant door.

Rural America has witnessed a precipitous decline in the number of ranches and farms with livestock over the last 30 years. In 1980 there were over 1.3 million ranches and farms with cattle across the country. Today, fewer than 950,000 are still in operation. In 1980 there were over 666,000 hog farms but according to the last USDA Hogs and Pigs Report [*USDA NASS Quarterly Hogs and Pigs Report – September 2010*] that number has declined by approximately 90% to fewer than 67,000.

For the first time ever, the 2008 Farm Bill included a Livestock title so that the integrity of the livestock and poultry market might be better restored, and the exodus of farmers and ranchers from livestock production halted or at least dramatically slowed. The 2008 Farm Bill included several specific directives for USDA and GIPSA including a directive to "promulgate regulations with respect to the Packers and Stockyards Act to establish criteria that the Secretary will consider in determining … whether an undue or unreasonable preference or advantage occurred in violation of the act."

The proposed GIPSA rule is an appropriate response to the call for regulatory action within the 2008 Farm Bill and follows both the authority to promulgate these rules that exists within the P&S Act as well as the intent of Congress in writing both of those laws. The Center for Rural Affairs supports the proposed rule and recommends its adoption as a final rule as soon as is practicable.

Competitive Injury

The P&S Act grants the Secretary the authority to write rules to enforce the Act. This authority has existed since 1921, when the Act was first made into law. In the proposed rule, GIPSA has included additional regulatory modifications under that existing authority extending from the P&S Act. These additions are also consistent with the intent of Congress in the 2008 Farm Bill and are well within the scope of the Secretary's existing authority under the Packers and Stockyards Act.

The proposed rule clarifies a number of definitions of terms within the P&S Act. Arguably, the definition for "undue or unreasonable preference" and the clarification of the application of "competitive injury" and "harm to competition" analyses in Section 202 cases are the heart of the matter in the proposed rule.

USDA has long argued that a violation of section 202(a) or (b) can be proven without proof of predatory intent, competitive injury or likelihood of injury to competition. The agency has not

been alone in that argument, the Center for Rural Affairs and a large number of other farm and rural organizations have long argued the same.

The courts, however, have struggled and stumbled in whether or not a "competitive injury" standard should be necessary to establish a violation of Section 202 of the P&S Act.

The proposed rule clarifies Section 202 of the P&S Act by offering additional language clearly stating that producers are required to prove merely one of the multiple prohibited actions by a packer in order to prove their grievance that a violation of the P&S Act has occurred. Farmers and ranchers will no longer be compelled to prove that damage done to them by a packer damages competition across the entire livestock sector.

In the absence of the interpretation established in the proposed rule, in order to obtain corrective action by packers who violate Section 202 of the P&S Act must demonstrate how the actions by which they were wronged have damaged competition throughout the entire sector. This is an enormous burden of proof, which is simply not substantiated by a plain reading of the Act and allows packers and processors to bully farmers and ranchers whenever it suits them to do so. Wronged producers should have access to judicial redress arising solely from the wrongful treatment. This proposed rule correctly adopts such a standard.

Justification for differential pricing or terms… required business information

The proposed rule establishes in Section 201.94 (B) that, "A packer, swine contractor or live poultry dealer must maintain written records that provide justification for differential pricing or any deviation from standard price or contract terms offered to poultry growers, swine production contract growers or livestock producers." The Center for Rural Affairs strongly supports this provision.

Justification of differential pricing is not an onerous burden to place on packers and processors. Packers and processors should maintain records of why major transactional business decisions, like differential pricing or terms, are made, just as any business operating with integrity would do.

Moreover, arbitrary and capricious punishments meted out to farmers and ranchers have resulted from simple expressions of free speech, including sharing contract terms with other producers or speaking out about market abuses by packers. Producers have good reason to want the Packers and Stockyards Administration to ensure that differential pricing and terms are legitimate business decisions, and not punitive.

However, reasonable justification for differential pricing or terms should not include so-called "operational efficiencies" that occur within the operation of the plant (beyond the point where slaughter begins… beyond the "knock-box," as it were). The internal plant operations should not be allowed as justification for volume-based premiums and they should never be allowed as any kind of justification for any action by packers or processors unless they are willing to keep records adequate for demonstrating to regulators and producers that these internal plant efficiencies are real and verifiable. Any declaration by a packer or processor that records about

such internal plant operations are proprietary business information should preclude those records or anything emanating from them from being used as a justification for differential pricing or terms.

The proposed rule defines and prohibits volume-based price discrimination, and rightly so. Rewarding high-volume producers – or punishing lower-volume producers – drives smaller-scale producers out of business. The proposed rule addresses this concern by prohibiting such price discrimination unless it is based on legitimate differences such as quality or timeliness. Enforcement of this crucial element of the rule depends on the requirement that packers and processors keep records that provide justification for differential pricing or terms.

Offering information to farmers, ranchers, regulators and other packers for reasonable review allows all parties to ascertain the validity and legitimacy of the packers' and processors' pricing strategies, especially in the absence of a less concentrated, less integrated and more competitive market place.

Producers, processors and retailers could maintain records in a manner of their choosing as long as the information is available and transferrable to a standardized format in the event of an audit by USDA. The data collected are merely business records that any other business would likely track, and, therefore, should not be considered onerous for any party.

Packer-to-Packer Sales

The proposed rule prohibits direct livestock sales between packers. The Center for Rural Affairs vehemently supports this administrative revision to the P&S Act regulations. While packers could still sell to individuals, dealers or other buyers, the rules do not ban packers from owning their own livestock, unfortunately. The Center for Rural Affairs believes that the P&S Act should prohibit packer ownership and custom feeding of livestock. In matter of fact, the Act was interpreted as prohibiting packer ownership and custom feeding of livestock from the inception of the law in 1921 until 1973, when USDA reversed that long-held interpretation.

The Center for Rural Affairs supports the proposed prohibition of packer-to-packer transactions. We also recommend that the provision be strengthened by prohibiting packers from owning their own livestock for more than 7 days prior to slaughter or engaging in custom feeding operations.

When nearly half the publicly reported transactions in the weekly hog trade are packer-to-packer sales, the potential for manipulation becomes severe. In fact, we know that such manipulation exists today. While USDA has made it clear that they do not believe that packer-to-packer sales are always intentionally price-manipulative, the potential for such manipulation is extreme. To allow for legitimate need of packer-to-packer transactions (e.g. plant shut-downs resulting in purchased livestock needing to be transferred to another facility, natural disasters, disease outbreaks, etc.), waivers for emergency sales could be made available to allow for orderly movement of livestock that have already been purchased through the system. This is reasonable.

However, more commonly, a plant will recognize during the day that workflow issues, stoppages or other matters have slowed the shift causing there to be a small excess of hogs, cattle or sheep

as the end of the shift nears. Likewise, shortages can occur as well when a shift operates above predicted capacity or perhaps when delivery of livestock is delayed. In some circumstances, especially for smaller packing plants, these situations can be alleviated by either delivering a small number of livestock to another plant or diverting scheduled delivery of incoming livestock to other plants. These are not unreasonable transactions, *per se*. But they should not be regular occurrences either.

The Center for Rural Affairs recommends that the rule be revised allowing for small lots of livestock (e.g. one or two potloads of cattle or hogs) to be traded (and reported) in packer-to-packer fashion to alleviate any concerns small packers have about managing their supply of livestock and for plant productivity issues in larger plants. We would suggest that no more than 400 hogs or 200 cattle should ever be sold by any one packer in packer-to-packer transactions in any given week. Further, no packer should be allowed to sell more than 600 hogs or 300 cattle in packer-to-packer transactions in any given month.

We also support the suggestion that other organizations have mentioned, namely, that the exemptions for small packers that exists under the mandatory price reporting statute be extended to this prohibition on packer-to-packer livestock transactions. We believe that the revision mentioned in the immediately preceding paragraph is a better solution, however.

Contracting Agreements

The proposed rule dramatically improves USDA's ability to enhance contract grower protection. The Center for Rural Affairs supports these provisions. Specifically, we believe that no contract will ever be ultimately fair to farmers if the packers and processors do not disclose all contract terms to all parties. We also believe that retaliatory contract termination, price reduction, providing substandard stock or feed, or denial of opportunity to remedy problems should be no less a violation of the P&S Act, no less "unjustly discriminatory" and perhaps no less of an "undue or unreasonable preference [or] disadvantage" than many of the actions described earlier when discussing hog and cattle markets.

It is a simple courtesy and a prudent business practice to provide someone entering into a contract the right to discuss the contract with their lawyer, financial advisor, family members or other confidants. Packer-producer contracts ought to be written in plain language. The common practice of creating intentionally-misleading and confusing contracts should end now.

The Center for Rural Affairs supports the provision in the rule that prohibits livestock and poultry integrators from requiring growers to make equipment changes if their existing equipment is in good working order, unless the company provides adequate compensation to the grower.

We also support new requirements in that rule that protect the substantial investments growers are required to make by their poultry companies, and to make sure they are not forced into making unwise investments, or retaliated against for not doing so. We support the provision requiring poultry contracts be long enough in term to allow growers to recoup at least 80 percent of the cost of their investments. Farmers bear the lion's share of the capital investment necessary

to produce livestock and poultry. It's unfair to allow packers, processors and integrators to pull the rug out from under them before they have recouped that investment, leaving them with nothing but debt and a highly specialized facility.

Lastly, contract producers should be allowed three days to review and cancel production contracts.

Conclusion

The Center for Rural Affairs urges Secretary Vilsack and Administrator Butler to strengthen the proposed rule in areas where they have received supportive suggested revisions and make the proposed rule a final rule and move toward implementation post-haste.

Overseeing America's livestock markets is one of the most thankless of jobs. However, family farmers and ranchers have learned that the absence of leadership in this role leaves governance to those who pursue power for their own narrow ends over the common good.

In the end, it comes down to this. In a nation where packers and processors own or control all of the livestock, from birth to slaughter, what need is there of farmers and ranchers? And what hope have we for revitalizing family farming, ranching and rural communities, if we have no hope of revitalizing family farm and ranch livestock production? What hope, if we cannot breathe life and competition back into our livestock markets?

My father always told me, "Say what you mean, and mean what you say." If we hope to create solutions to some of the challenges that family farmers, ranchers and rural communities face, then we should all support this proposed rule and the livestock market reforms contained therein… in other words, we should mean what we say.

Progress comes when people of hope and vision put good ideas on the table of governance. Secretary Vilsack and Administrator Butler have put a picked up a good idea and carried it forward. We urge them to have the hope and vision to take the final step.

Thank you for the opportunity to comment on this important matter. The Center for Rural Affairs looks forward to answering any further questions that may arise and will be happy to help as needed with the revisions and implementation process of this proposed rule.

Sincerely,

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