

The Role of Economic and Legal Analysis in the GIPSA Rules Debate

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The Packers and Stockyards Act (PSA) is 89 years old, but its most recent year may be its most contentious. The PSA and its administering agency, the U.S. Department of Agriculture's Grain Inspection, Packers and Stockyards Administration (GIPSA), found themselves thrust into the spotlight on June 22, 2010 when GIPSA published a set of proposed rules to "describe and clarify conduct that violates the PSA and allow for more effective and efficient enforcement by GIPSA." Some groups say the proposed rules are much-needed changes, while others maintain the rules could cause costly disruptions to the structure of the livestock marketing system. This article examines the proposed GIPSA regulations, the debate surrounding them, and what these deliberations may mean for the livestock industry and the policy formation process.

The Rules: Past, Present, and Possibly Future

Ensuring fairness in livestock and poultry markets is the fundamental purpose of the PSA. While the PSA and its supporting regulations employ a number of provisions to accomplish this purpose, one particular requirement sets the stage for the current controversy. Under the PSA, packers, swine contractors, and live poultry dealers—more commonly known as "integrators"—integrators are prohibited from using "any unfair, unjustly discriminatory, or deceptive practice or devices." The ambiguity of this language led to numerous lawsuits as courts tried to lend it meaning. Eventually, a line of cases emerged requiring a livestock producer to prove not only that he or she had been individually harmed by a packer or integrator's behavior, but also that the behavior caused harm to the competitiveness of the industry as a whole.

Hoping to resolve this and other controversies surrounding the PSA, the Food, Conservation, and Energy

Act of 2008 (2008 Farm Bill) directed the USDA to enact rules clarifying the PSA. Specifically, Section 11006 of the 2008 Farm Bill required the USDA to establish criteria to determine:

- (1) whether an undue or unreasonable preference or advantage has occurred in violation of [the PSA];
- (2) whether a live poultry dealer has provided reasonable notice to poultry growers of any suspension of the delivery of birds under a poultry growing arrangement;
- (3) when a requirement of additional capital investments over the life of a poultry growing arrangement or swine production contract constitutes a violation of such Act; and
- (4) if a live poultry dealer or swine contractor has provided a reasonable period of time for a poultry grower or a swine production contract grower to remedy a breach of contract that could lead to termination of the poultry growing arrangement or swine production contract.

GIPSA responded with a notice of proposed rulemaking on June 22, 2010. GIPSA not only addressed the requirements of the 2008 Farm Bill, but also addressed a number of other issues, citing the language of the PSA granting GIPSA broad authority deal with "packers, stockyards, marketing agents and dealers." The expansion of the rules' scope beyond that of the Farm Bill language did not escape notice, and has become one of numerous points of contention between the agency and those opposed to the rule.

Discussing the potential impacts GIPSA's proposal requires a brief overview of the proposed regulations. These rules are grouped in Table 1 according to the section of the PSA cited by GIPSA as authority for proposing those rules.

Table 1: Proposed GIPSA Regulations

| NOTES: P = poultry, S= swine, C = cattle Unless otherwise noted, all references are to the Code of Federal Regulations, Title 9 | | |
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| Rule | Species Affected | Proposal |
| 7 U.S.C. §192(a) – “unfair, unjustly discriminatory or deceptive practices or devices” | | |
| 201.210(a) [new] | P,S,C P,S,C P,S P,S,C S,C P,S P,S,C P,S,C | Defines eight items as per se “unfair”: (1) unjustified breach of contractual duty or other act/omission reasonably determined to be unscrupulous, deceitful, or in bad faith; (2) retaliatory act/omission in response to a producer’s act of expression (ex. comments by grower or joining an association); (3) refusal to provide producer with data used to calculate producer’s compensation; (4) attempting to contractually limit producer’s legal remedies, including right to trial by jury, right to damages provided by law, bankruptcy rights, potential attorneys fees, and restrictions on venue of trial or arbitration; (5) providing a premium or discount to a producer without documenting the justification; (6) terminating a contract based on a producer’s alleged violation of a law, unless the violation was reported to the applicable authorities; (7) representations, acts, or omissions likely to mislead a producer regarding contracts or transactions; and (8) any act causing or creating “competitive injury” or a “likelihood of competitive injury”. |
| 201.2(n),(o) [modified] | P,S | Defines “capital investment” and “additional capital investment” as initial or additional investments of \$25,000 or more in growing and raising facilities. |
| 201.217 [new] | P,S,C | (1) If producer is required to make new or additional capital investment, contract must be for sufficient length of time to allow producer to recoup 80% of investment; (2) Producers cannot be penalized (by animal placement reduction or contract termination) for not making equipment changes when existing equipment is in “good working order”; (3) Producers may not be intimidated or mislead into entering into production contract; (4) Cannot require additional capital investment if producer has given notice of intent to sell; and (5) Cannot require equipment changes without “adequate compensation incentives”. |
| 201.215 [new] | P | Poultry producers must be given reasonable notice prior to suspension of delivery of birds. Factors include whether notice is in writing, if it was given at least 90 days prior to suspension, and if notice included reason for and length of the suspension and date delivery of birds will resume. |
| 201.218 [new] | P,S | Producers must be given reasonable time to cure breach of production contract. Failure to provide written notice of the breach within 90 days of discovery would be generally considered waiver of breach. Written notice must include: (1) description of the act/omission constituting the breach; (2) when breach occurred; (3) how breach can be remedied; and (4) date by which the breach must be remedied. |
| 7 U.S.C. §192(b) – “undue or unreasonable preference or advantage” | | |
| 201.212 [new] | C | Packer-to-packer sales prohibited (except emergency waiver). Requires livestock dealers in exclusive arrangement with a packer to be identified as “packer buyer.” Once identified, dealers can only purchase livestock for that packer. |
| 201.213 [new] | P,S,C | Sample copies of all forward, formula and production contracts, marketing agreements, and poultry growing arrangements must be submitted to GIPSA for online posting (after redaction of confidential information); 10 day window for submission once agreement is used, and 10 day window for notification of stoppage of use. |
| 201.214 [new] | P | Addresses “tournament system” in poultry production; all growers raising the same type and kind of poultry must be given same base pay, and compensation may not be reduced below the base pay rate. Growers may only be ranked with other growers who use the same house type. |
| 201.94 [modified] | P,S,C | Packers, swine contractors or poultry dealers paying different prices or giving different contract terms to different producers must keep written records documenting the rationale for the difference. |

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| 201.211 [new] | P,S,C "Producer" "Livestock" | Lists factors to be considered in determining whether an "undue or unreasonable preference or advantage or an undue or unreasonable prejudice or disadvantage" has occurred. (1) Were contract terms based on number or volume of animals made available to all producers who could provide similar numbers or volumes of animals? (2) Were price premiums based on quality, time of delivery, and production methods made available to all producers who could meet the same specifications? (3) Was information regarding the acquisition, handling, processing and quality of livestock disclosed equally? |
| 7 U.S.C. §197 – the use of arbitration in contracting | | |
| 201.219(a) [new] | P,S,C | Lists factors to be considered in determining whether arbitration clause allows producer a "meaningful opportunity" for participation in the arbitration process. Contractual disclosures include: (1) amount to be paid by the producer in the arbitration process and any limitations on the producer's legal remedies (in bold, conspicuous print); (2) whether impartial "neutrals" will be used as arbitrators; (3) comparison of costs relative to typical employer/employee arbitration; (4) time limits associated with the arbitration process; (5) the compliance of the procedure with the Federal Arbitration Act; (6) the ability of the producer to access information held by the packer, swine contractor or live poultry dealer; (7) the purposes for which arbitration can be used; and (8) the provision of a written arbitration opinion based on law and precedent. |
| 201.219(b) [new] | P,S,C | Arbitration language must be followed by a clause granting producer the right to decline the arbitration provisions of the contract using language specifically laid out in proposed regulations. |

A Curious Conversation

Under the Administrative Procedure Act (APA), GIPSA established August 23, 2010 as the deadline for the public to submit comments on the proposed rule and almost immediately, a vigorous discussion ensued. Calls went up for more time to evaluate the rule and its implications. In a move many believe to have been prompted by the extraordinary interest in the rule by both the livestock industry and by several members of Congress, GIPSA extended the comment deadline to November 22, 2010.

Overlapping the comment period for the proposed rule, the USDA and the Department of Justice ("DOJ") conducted a series of workshops regarding "Agriculture and Antitrust Enforcement Issues in our 21st Century Economy" from March to December of 2010, with two workshops occurring before the publication of the initial rule, and one workshop held after the extended comment period had concluded. Portions of

the two workshops held during the comment period (June 25th in Madison, Wisc. and August 27th in Fort Collins, Colo.) allowed time in their agendas for public comments, but the events were not generally publicized as hearings on the proposed rule itself, leading to confusion both in the comments offered and on the part of those making the comments as to how their statements would be regarded by the agency.

At the same time, several members of Congress appeared taken aback by the scope of the proposed rules beyond the specific language of the 2008 Farm Bill and the reasons additional analysis of the rules' impact was not forthcoming. In a July 20th hearing before the Livestock, Dairy and Poultry Subcommittee, GIPSA administrators were asked why the comment period would not be extended until the completion of all the USDA/DOJ workshops and requested a 120 day extension of the comment period (the actual extension eventually granted by GIPSA

was 90 days). Eventually, 115 Congressmen jointly signed a letter to USDA Secretary Vilsack on October 1, 2010 citing the scope of the rule as exceeding the language of the 2008 Farm Bill and requesting the USDA Chief Economist to perform a thorough analysis of the economic impact of the rule.

While the comment period has concluded, the debate continues. As of the date of this writing, the record contains over 66,000 comments.

Will They Throw the Challenge Flag?

Everyone engaged in the discussion seems to agree on one thing: if implemented in their current form, the regulations will create significant industry changes. While some believe that the need for the rules is self-evident and requires no further study, others believe the proposed rules ignore what current scholarship suggests for improving the livestock industry. Thus, just as millions of football fans

simultaneously scream for a replay of a call they think went awry, many livestock and poultry industry participants think the proposed rules warrant further review. Most commonly, those calls arise from questions about the economic impact of the rule, its potential to change industry legal standards, and questions about how GIPSA will enforce its provisions.

Economic Analysis

One reason cited among those saying the rule needs closer scrutiny is a desire to better understand the changes it will trigger for both the agricultural economy. In the proposed rule, GIPSA acknowledged that the rule was “significant” as defined by Executive Order 12866 which implies an estimated economic impact of \$100 million or more, but the economic analysis provided within the rule is, by most accounts, quite sparse. Notably absent from the proposed rules’ economic analysis section are any significant discussions of a number of GIPSA-funded studies on concentration in the livestock and poultry industries including the 1996 six-university industry packing concentration study and a 2007 Congressionally-ordered study of alternative marketing arrangements. However, neither of these GIPSA-administered studies were referenced in the rule. The omission of these studies surprised many scholars, as they were regarded as the most comprehensive studies on the topic of market concentration and the impact of alternative marketing arrangements (AMAs).

The 1996 study was a vast and intensive examination of concentration in the meatpacking industry, including studies of market data—including GIPSA data, surveys of feeders and packers, and a comprehensive review of the literature on the topic. The study showed no conclusive evidence that firms were using market power in any significant way. The study also recommended “future surveillance and analysis” of contract-

ing arrangements and other forms of coordination. Following the 1996 study, the 2007 study focused on the use of AMAs in the red meat industry. It showed that the industry relied increasingly on AMAs to coordinate production, and that “restrictions on the use of AMAs for sale of livestock to meat packers would have negative economic effects on livestock producers, meat packers, and consumers.” In effect, the 2007 study found that restricting the use of AMAs would trigger a cascade effect, especially in the beef industry: restricting the use of AMAs would increase costs to packers and force them to secure cattle with a broader range of quality traits, which would reduce the quality of beef slaughtered, reduce beef demand, and eventually have negative impacts to packers, feeders, cattle producers, and even consumers. The conclusion of the study with regard to the beef industry: “The cost savings and quality improvements associated with the use of AMAs outweigh the effect of potential oligopsony market power that AMAs may provide packers.” In other words, restricting AMAs would likely cause more harm than good.

The conclusions from these studies have led to much of the industry concern about the rules’ potential impact. For example, proposed 9 C.F.R. § 201.210(a)(5) would require documentation of the economic justification for paying a premium or discount to livestock producers. Many industry observers believe this provision will lead to a reduction in the use of AMAs and an increase in the use of cash markets—a situation almost identical to that modeled in the 2007 study. However, wide differences exist in the analyses applied by different groups in their estimation of how far these impacts may range. For example, GIPSA states: “Because these regulations merely clarify existing requirements, any such costs must be incurred regardless of whether the regulations are issued,

and are therefore not costs associated with the regulations themselves.” A group opposing the proposed rules, the American Meat Institute, looks at this provision differently, though, assuming that this provision will drive packers to abandon alternative marketing arrangements altogether and thus cause a \$14.0 billion loss to GDP. The authors’ intent is not to say either number is wrong, but rather to underscore that an information gap exists between the two sides. Additionally, while several groups critical of the rule—including the National Pork Producers Council, the National Cattlemen’s Beef Association, and the National Chicken Council—prepared economic studies indicating significant negative impacts, groups in favor of the rule have not advanced studies to the opposite effect. This is understandable since the burden of proving the economic viability of a regulation rests with the agency proposing it. GIPSA has recently attempted to address this matter though, announcing on December 13th—after the close of the comment period—that USDA would conduct a more detailed cost-benefit analysis of the rule.

Shift in Legal Standards

Another significant point of debate comes from the potential addition of 9 C.F.R. §201.2(t) and (u) which would define “competitive injury” and “likelihood of competitive injury,” respectively. Historically, to make a claim that a practice violated the PSA’s prohibition of unfair marketing behavior, a party had to show that the practice caused “competitive harm” under the meaning of that term in antitrust law: the behavior caused harm to the competitive balance of the industry as a whole. Although the PSA itself does not define “competitive harm,” case law evolved to accept the antitrust definition of the term, with eight federal circuit courts concurring in the interpretation.

Removing a requirement to show that market behavior harms the industry as a whole lowers a significant barrier to lawsuits under the PSA. Whether that represents a benefit or cost depends largely upon one's perspective. Some livestock and poultry producers have voiced support for this portion of the proposed rule as greatly improving their access to the courts, while on the other side of the same coin, packers and integrators have expressed concern about a sharp increase in PSA enforcement and civil litigation as a result.

Rule Implementation and GIPSA's Enforcement

Admittedly, one cannot predict the economic or legal impacts of a proposed rule without understanding how it will impact the day-to-day operations of the livestock and poultry industry. For example, proposed 9 C.F.R. § 201.212 would govern the operations of “packer buyers” in exclusive arrangements with packers—notably, while a definition of “packer buyer” appears in the rules' preamble, it does not appear in the actual language of the rule itself. GIPSA's analysis indicates that this change would only affect cull cattle auctions, but the rule itself does not limit its impact to those markets. Will this change reduce tacit collusion by packers, or will it reduce the number of buyers causing the closure of some small markets and actually increase concentration in the cash markets?

Another cause of uncertainty in the industry comes from the provisions of proposed 9 C.F.R. §§ 201.94 and 210(a)(5) requiring packers, swine contractors, and live poultry dealers to maintain documentation “providing justification for differential pricing or any deviation from standard price or contract terms.” Neither the language of the rule nor GIPSA's preamble analysis indicates the documentation required under this rule, nor does it define the term “standard price or contract terms.” Could

a packer draft one standard “pricing manual” that covers all contingencies of pricing or would it be required to maintain separate documentation for each transaction in which a non-standard price was paid? Could such a manual satisfy the intent of the new rules where price premiums and discounts over a base price may need to change on an hour-by-hour or even minute-by-minute basis? The answer drives a significant portion of the debate around the rules. As mentioned above, many industry groups think that the requirement of individual documentation would make the use of alternative marketing arrangements impractical, but if general documentation is all that is required, there might be little to no reduction in the use of such tools.

Contradictions within the rule also cloud the debate. Some legal analysts have observed that proposed 9 C.F.R. §§ 201.94 and 210(a)(5) are incompatible with proposed § 201.211, since the former requires documenting justification for price differentials and the latter could be read to functionally prohibit price differentials. The preamble also references proposed 9 C.F.R. § 201.210(c) which purports to govern analysis of the interpretation of the PSA's seminal provisions, but no § 201.210(c) appears in the rule itself.

Where Do We Go from Here?

GIPSA now faces the decision of implementing the rule as currently proposed, modifying it, or “going back to the drawing board.” If enacted as written, the rule will doubtless cause changes in the industry. The question, of course, is what specific changes will occur. That question may be answered in a clarified final rule; if not, it will be resolved through what will likely be a torrent of litigation. Regardless of how the issue is finally resolved, three themes arise from the discussion surrounding these rules.

First, the traditional “party lines” in the landscape of agricultural policy

debate are shifting. Many livestock and poultry disputes come down to the “us versus them” paradigm of producers versus integrators, but some of the loudest voices both for and against the proposed regulations come from livestock and poultry producers themselves. Producer-proponents of the rule hold that it will bring balance, transparency, and fairness to the livestock and poultry markets, while producer-opponents say it will scuttle years of their efforts to differentiate their product from other producers and in so doing reduce their ability to capture a bigger portion of the food dollar.

Second, this debate leaves many stakeholders wondering whether accountability for the current situation lies with Congress or with USDA. Whatever stance one takes with respect to the proposed rule, it seems clear that in its current form, the rule will have profound impacts on the livestock industry, and perhaps on the entire agricultural sector. Some argue that such sweeping changes were never intended to be the domain of agencies, but were instead left to Congress. Congress may argue that it directed GIPSA to address the issue narrowly and that GIPSA exceeded its mandate, but one may also note the relative silence of Congress while the PSA was debated in the courts. Others argue the increasing complexity of the marketplace requires agencies to take on an ever-growing role in policy. If that is the case, though, stakeholders face the question of how to hold appointed officials, rather than elected legislators, accountable for their actions. Regardless of which perspective prevails, it is incumbent upon all industry participants—and indeed, are not all Americans participants in some industry—to become increasingly well-informed, increasingly involved in policy, and increasingly shrewd in their advocacy.

This leads us to the third point: such a policy environment demands rich and thorough debate informed by

objective research. That environment has not yet developed, though, largely due to two factors. First, much of the current discussion has been framed only by partisan analyses, and regardless of how thorough and objective they may be, studies put forth by any industry group face perceptual credibility issues. Sound, objective research on the effects of industry structure changes in the livestock and poultry sector is already available. Policy makers and industry groups should both be encouraged to avail themselves of these resources, and researchers should increase their efforts to engage both sectors and communicate the implications of their findings. Second, much of the current debate is clouded by an incomplete picture of the practical implementation of the proposed regulatory changes. Resolving this concern requires a true dialogue between regulator and regulated party, enabling the regulator to see first-hand the daily operations of the regulated party and allowing the regulated party to understand clearly the outcomes desired by the regulator.

For More Information

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