

MINUTES OF THE HOUSE COMMITTEE ON AGRICULTURE.

The meeting was called to order by Chairman Dan Johnson at 3:30 p.m. on February 24, 2003, in Room 423-S of the Capitol.

All members were present except:

Committee staff present:      Raney Gilliland, Legislative Research Department  
   Gordon Self, Revisor of Statutes Office  
   Kay Scarlett, Committee Secretary

Conferees appearing before the committee:

Don Teske, President, Kansas Farmers Union  
Malcolm Moore, Director, R-CALF  
Mike Schultz, Executive Director, Kansas Cattlemen's Association  
David Pfrang, Goff, Kansas  
Steve Cady, Executive Director, Organization for Competitive Markets  
Mike Beam, Senior Vice President, Kansas Livestock Association  
Larry Jones, President, Kansas Livestock Association (written only)  
Tracy Brunner, Ramona, Kansas  
Patrick Hubbell, Tyson Foods, Inc. (IBP)  
Leslie Kaufman, State Director, Governmental Relations, Kansas Farm Bureau

Others attending:      See attached list

Minutes of the February 17 and 18 meetings were distributed. Members were asked to notify the committee secretary of any corrections or additions prior to 5:00 p.m. February 26, or the minutes will be considered approved as presented.

**Discussion and action on HB 2168 - Preservation of historic property consistent with farming and ranching operations.**

Chairman Johnson opened discussion on **HB 2168**. Raney Gilliland explained that the language in the original bill would exempt persons proposing changes to land within 500 feet of a historic property if those changes are consistent with generally accepted agricultural practices. The committee was reminded that a **Proposed Substitute for HB 2168** was discussed at the hearing that would remove all environs language and codify the practice of the Historical Society that no property is placed on the state register without the support and approval of the landowner.

A **second Proposed Substitute for HB 2168** was distributed. In addition to the changes proposed in the first substitute proposal, this version would remove the requirement that the State Historical Society maintain a listing of historic places on the national register of historic places and would delete the term "encroach upon" from the language of the bill. (Attachment 1)

Representative Dahl moved to recommend the second Proposed Substitute for HB 2168 favorable for passage. The motion was seconded by Representative Ostmeyer. Committee discussion ensued.

Representative Thimesch moved to table HB 2168. Seconded by Representative Showalter, the motion carried.

**Hearing on HB 2167 - Prohibiting ownership of livestock by packers.**

Chairman Johnson opened the hearing on **HB 2167**. Raney Gilliland explained that this bill would prohibit a packer from directly or indirectly owning livestock for the production of livestock or livestock products,

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except that temporary ownership would be allowed for 14 days prior to slaughter. The bill defines livestock as live cattle or swine and a packer as someone engaged in the business of slaughtering livestock in Kansas in excess of 1.0 million animal units per year. The bill would also impose limitations on the pricing of livestock. Violations would be handled by the Attorney General or county or district attorney.

Don Teske, President, Kansas Farmers Union, spoke in support of **HB 2167** to ban packer ownership of livestock. Kansas Farmers Union believes prohibiting packer ownership of livestock is important in restoring competitive and healthy agricultural markets. Although this is a national issue, he said that sometimes federal policy shifts have to be directed by state mandates. ([Attachment 2](#))

Malcolm Moore, Director, R-CALF, testified in support of **HB 2167**. He reported that five other states currently have bans on packer ownership and that the U.S. Senate passed a ban on packer ownership that was stripped in conference committee last year. Neither Kansas Senator voted for the ban when it passed the full Senate. ([Attachment 3](#))

Mike Schultz, Executive Director, Kansas Cattlemen's Association, appeared in support of **HB 2167**. Copies of a Beef Study dated July 29, 2002, conducted by a research firm in Dodge City is included with his testimony. ([Attachment 4](#)) An article on *The 2002 Senate Farm Bill: The Ban on Packer Ownership of Livestock* written by agricultural lawyers, Associate Professor Dr. Roger McEowen from Kansas State University, Dr. Peter Carstensen from the University of Wisconsin, and Dr. Neil Harl from the University of Iowa, published in the Drake Journal of Agriculture Law was also provided.

David Pfrang, Goff, Kansas, testified in support of **HB 2167** to provide an open and competitive marketplace, free from undue influences by the packing sector. ([Attachment 5](#))

Steve Cady, Executive Director, Organization for Competitive Markets, appeared in support of **HB 2167**. OCM works on issues of market power, market structure and market conduct. The written testimony of Michael C. Stumo, legal counsel for the Organization for Competitive Markets, presented to the U. S. Senate Committee on Agriculture, Nutrition and Forestry on July 16, 2002, is included with his testimony. ([Attachment 6](#))

Mike Beam, Senior Vice President, Kansas Livestock Association, appeared in opposition to **HB 2167**. KLA is opposed to **HB 2167** because the bill (1) would restrict and/or prohibit marketing arrangements currently used by their members; (2) would impose state marketing guidelines that would be inconsistent with, and in contrast to, existing federal rules governed by USDA; and (3) likely would violate the Commerce Clause of the United States Constitution. ([Attachment 7](#))

Larry Jones, President, Kansas Livestock Association, submitted written testimony in opposition to **HB 2167**. He reported that it was the consensus of a Four-State Working Group, including KLA, Texas Cattle Feeders Association, Colorado Livestock Association, Nebraska Cattlemen's Association and the Kansas Cattlemen's Association, that getting the government involved in deciding who can own cattle was not the answer. He reported that South Dakota and Missouri have tried similar legislation with disastrous effects on producers. He noted that a federal court recently ruled an Iowa law banning pork processors from directly or indirectly owning, operating, or controlling pork production unconstitutional in violation of the Commerce Clause of the United States Constitution. ([Attachment 8](#))

Tracy Brunner, Ramona, Kansas, appeared as an opponent to **HB 2167**. He believes that any law beyond what is currently in effect at the federal level will stymie innovation and limit future marketing opportunities. ([Attachment 9](#))

Patrick Hubbell, representing Tyson Foods, Inc. (IBP), testified in opposition to **HB 2167** stating that it would violate the Interstate Commerce Clause of the U.S. Constitution as similar legislation did in Iowa. He said that prohibiting packer ownership could cause financial detriments to those independent producers who raise livestock for packers under contract and have financed their operations based on those contracts. He noted that almost all contracts that Tyson/IBP enters into with producers are requested by producers. Forced liquidity of livestock and livestock operations by the packers could also have negative impacts. He thought

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MINUTES OF THE HOUSE COMMITTEE ON AGRICULTURE at 3:30 p.m. on February 24, 2003, in Room 423-S of the Capitol.

that such a law would be more appropriate at the federal level in order to avoid violations of ICC or to put producers in one state at a disadvantage over other states. (Attachment 10)

Leslie Kaufman, State Director, Governmental Relations, Kansas Farm Bureau, discussed **HB 2167** and American Farm Bureau Federation policy concerning packer ownership of cattle and swine and base pricing in formula and grid pricing arrangements. In January 2003, AFBF removed policy language to prohibit packer ownership of livestock for more than 14 day prior to slaughter. Thus, Kansas Farm Bureau does not support a ban on packer ownership of livestock. AFBF did approve language that contracts and marketing agreements should specify a negotiated base price before commitment to delivery. Therefore, Kansas Farm Bureau does partially support this concept—the significant difference is that AFBF policy is permissive and the bill is mandatory. KFB likes the fact that enforcement is vested in the court system and not administrative procedures. (Attachment 11)

The hearing on **HB 2167** was closed.

The Chairman announced that the House Committee on Agriculture will be meeting informally at noon on Wednesday, March 5, in Room 423-S. Dr. Ralph Richardson, Dean of the College of Veterinary Medicine will provide an update on the veterinary program at Kansas State University.

The meeting adjourned at 5:30 p.m. The next regular meeting is scheduled for March 5, 2003 at 3:30 p.m. in Room 423-S.

# HOUSE AGRICULTURE COMMITTEE GUEST LIST

DATE: February 24, 2003

NAME	REPRESENTING
Tom Bruno	Farm Credit
Pat Hubbell	YHS (IBP)
Dag Wareham	KGFA/KARA
Carol von Hirsch	Lawrence Res. Alliance
Shelley King	KS Atty. Gen.'s office
Al Ziser	
Terry Haddock	Mo Livestock Assn & Cattle Feeders
Mike Beem	Ks. Livestk Assn
Jacy Bunn	Cow Camp Inc.
DORT Goodman	OCM
David Phoenix	KCA
Don M. Regan	KCA
Donn Teske	Ks Farmers Union
Robert Schroeder Jr	KCA
Gerry J. Coy	K.C.A.
Sally Hatcher	Kansas Preservation Alliance
Wanda Kenney	KCA
Christy Davis	Kansas State Historical Society
Mary Allman	Kansas State Historical Society

# HOUSE AGRICULTURE COMMITTEE GUEST LIST

DATE: February 24, 2003

NAME	REPRESENTING
<i>Michael L. Schultz</i>	<i>KANSAS CATTLEMENS ASSN.</i>
<i>Richard L. Roesch</i>	<i>Kansas cattlemen's assn.</i>
<i>Richard Penkatz</i>	<i>Ks State Historical Society</i>
<i>Leslie Kaufman</i>	<i>Ks Farm Bureau</i>
<i>Michael A. Di</i>	<i>KFB</i>

## Proposed Substitute for HOUSE BILL NO. 2168

By

AN ACT concerning state historic property; relating to approval of owner for listing of property on state register; notice provisions; amending K.S.A. 75-2721 and K.S.A. 2002 Supp. 75-2724 and repealing the existing sections.

Be it enacted by the Legislature of the State of Kansas:

Section 1. K.S.A. 75-2721 is hereby amended to read as follows: 75-2721. (a) The state historical society shall have the following historic preservation powers and duties:

(1) Undertake a statewide survey to identify and document historic properties, including all those owned by the state, its instrumentalities and political subdivisions.

(2) Prepare and maintain a state register of historic places, ~~which shall include all those listed on the national register of historic places.~~ The historical society shall adopt standards for the listing and maintenance of historic properties on the state register consistent with relevant federal standards for preservation and care of historic properties. Such standards shall include a requirement that approval of the owner of the property is required before the listing of the property on the state register of historic places.

(3) Prepare the state's preservation plan, review such plan annually and make appropriate revisions.

(4) Within limits of available resources, acquire historic properties by gift, purchase, devise or bequest; preserve, restore and administer such properties; and transfer such properties when authorized by law.

(5) Establish standards and criteria for the acquisition of historic properties and for the preservation, restoration, maintenance and operation of properties under the jurisdiction of the agency, and, when deemed proper, to charge reasonable admission fees to such properties.

(6) Undertake the procedures necessary to qualify the state for participation in sources of federal aid for historic preservation purposes.

(7) Provide information concerning historic properties

within the state to the agencies and instrumentalities of the federal, state and local governments and, where appropriate, to private individuals and organizations.

(8) Cooperate with federal, state and local government agencies in the planning and conduct of specific undertakings affecting historic properties and preservation objectives and in overall land-use planning.

(9) Disburse federal and state funds to local governments and private agencies and individuals for historic preservation work; establish standards of eligibility to receive such funds; and enter into maintenance agreements with local governments and private agencies concerning historic properties.

(10) Participate in national and international conferences and programs concerning historic preservation and cooperate with federal officials and agencies in the conduct of such activities.

(11) Subject to limitations of staff and resources, provide technical and financial assistance to local historic preservation organizations and private parties involved in historic preservation activities.

(12) Assist, where possible, in developing public interest in historic preservation through the development and implementation of interpretive programs for historic properties and through the management of the state's historical marker program.

(13) Develop an ongoing program of historical, architectural and archeological research and development, to include continuing surveys, excavation, scientific recording, interpretation and publication of the state's historical, architectural, archeological and cultural resources. A reasonable charge may be made for publications.

(14) Request that the attorney general take action authorized under subsection (d) of K.S.A. 75-2724 and amendments thereto against any person or entities who fail to obtain any demolition or building permit required by local or state law.

(b) The state historic preservation officer shall adopt

rules and regulations to implement and administer the provisions of K.S.A. 75-2715 through 75-2725, and amendments thereto.

Sec. 2. K.S.A. 2002 Supp. 75-2724 is hereby amended to read as follows: 75-2724. (a) The state or any political subdivision of the state, or any instrumentality thereof, shall not undertake any project which will encroach--upon, damage or destroy any historic property included in the national register of historic places or the state register of historic places ~~or the environs of such property~~ until the state historic preservation officer has been given notice, ~~as provided herein,~~ and an opportunity to investigate and comment upon the proposed project. ~~Notice to the state historic preservation officer shall be given by the state or any political subdivision of the state when the proposed project, or any portion thereof, is located within 500 feet of the boundaries of a historic property located within the corporate limits of a city, or within 1,000 feet of the boundaries of a historic property located in the unincorporated portion of a county. Notwithstanding the notice herein required, nothing in this section shall be interpreted as limiting the authority of the state historic preservation officer to investigate, comment and make the determinations otherwise permitted by this section regardless of the proximity of any proposed project to the boundaries of a historic property.~~ The state historic preservation officer may solicit the advice and recommendations of the historic sites board of review with respect to such project and may direct that a public hearing or hearings be held thereon. Any such public hearing or hearings held pursuant to this subsection or held pursuant to authority delegated by the state historical preservation officer under subsection (e) or (f) shall be held within 60 days from the date of receipt of notice by the state historical preservation officer from the state or any political subdivision of the state as provided herein. If the state historic preservation officer determines, with or without having been given notice of the proposed project, that such proposed project will encroach--upon,



damage or destroy any historic property included in the national register of historic places or the state register of historic places ~~or--the-envirens-of-such-property~~, such project shall not proceed until:

(1) The governor, in the case of a project of the state or an instrumentality thereof, or the governing body of the political subdivision, in the case of a project of a political subdivision or an instrumentality thereof, has made a determination, based on a consideration of all relevant factors, that there is no feasible and prudent alternative to the proposal and that the program includes all possible planning to minimize harm to such historic property resulting from such use; and

(2) five days notice of such determination has been given, by certified mail, to the state historic preservation officer.

(b) Any person aggrieved by the determination of the governor pursuant to this section may seek review of such determination in accordance with the act for judicial review and civil enforcement of agency actions. Any person aggrieved by the determination of a governing body pursuant to this section may seek review of such determination in accordance with K.S.A. 60-2101 and amendments thereto.

(c) The failure of the state historic preservation officer to initiate an investigation of any proposed project within 30 days from the date of receipt of notice thereof shall constitute such officer's approval of such project.

(d) Failure of any person or entity to apply for and obtain the proper or required building or demolition permit before undertaking a project that will ~~encroach-upon~~ damage or destroy any historic property included in the national register of historic places or the state register of historic places, or the environs of such property, shall be subject to a civil penalty not to exceed \$25,000 for each violation. The attorney general may seek such penalties and other relief through actions filed in district court.

(e) (1) The state historic preservation officer may enter

into an agreement authorizing a city or county to make recommendations or to perform any or all responsibilities of the state historic preservation officer under subsections (a), (b) and (c) if the state historic preservation officer determines that the city or county has enacted a comprehensive local historic preservation ordinance, established a local historic preservation board or commission and is actively engaged in a local historic preservation program. The agreement shall specify the authority delegated to the city or county by the state historic preservation officer, the manner in which the city or county shall report its decisions to the state historic preservation officer, the conditions under which the city or county can request assistance from the state historic preservation officer in performing certain project reviews, the length of time the agreement is to be valid and provisions for termination of the agreement. Such agreement shall provide that the state historic preservation officer shall retain final authority to implement the provisions of this act. The state historic preservation officer shall adopt any rules and regulations necessary to implement the provisions of this subsection.

(2) An agreement with a city or county authorized by this subsection shall not be construed as limiting the authority of the state historic preservation officer to investigate, comment and make determinations otherwise permitted by this section.

(f) The state historic preservation officer may enter into agreements with the state board of regents or any state educational institution under the control and supervision of the state board of regents to perform any or all responsibilities of the state historic preservation officer under subsections (a), (b) and (c).

Sec. 3. K.S.A. 75-2721 and K.S.A. 2002 Supp. 75-2724 are hereby repealed.

Sec. 4. This act shall take effect and be in force from and after its publication in the statute book.

House Ag Committee hearing on HB 2167

An Act concerning livestock: relating to ownership of such livestock by packers:  
prescribing penalties therefor.

Testimony by Donn Teske,  
Kansas Farmers Union President  
2-24-03

Good afternoon, I am Donn Teske, President of the Kansas Farmers Union. I wish to speak today in support of HB 2167. Kansas Farmers Union as well as our umbrella organization, National Farmers Union has been a strong advocate for enacting a "ban on Packer ownership". Both state and national FU's have strong language in our policy asking for a ban. During the farm bill debates this past year more than 30 farm organizations were calling for completion of a farm bill which included a federal ban on packer ownership.

Why do we think a ban on ownership is needed? We believe that as market control of the livestock industry becomes more concentrated that a few entities controlling the slaughter while using captive, owned supplies distorts the true cash market. In a Jan 30<sup>th</sup> 2002 NFU press release, our president Leland Swenson said "Our nation's farmers, ranchers and independent feedlot owners want competition in the marketplace", he said "Packers who own livestock can use their own animals to immediately depress livestock market upturns. Self-dealing by packers restricts and often eliminates the ability of small- and medium-sized producers to access the market". "Prohibiting packer ownership of livestock is important in restoring competitive and healthy agricultural markets", Swenson said. "If individual family farms and ranches are to survive, legislation must be enacted to stop current trends that increase market power for only a few". As reference to support Farmers Union Policy, I would like to direct the members of this committee to a paper prepared by Roger McEowen, of Kansas State University, Peter Carstensen, and Neil Harl titled "The 2002 Senate Farm Bill: The ban on Packer Ownership of Livestock." This paper does an excellent job of documenting the increased use of ownership control of livestock through the 1990's and the detrimental spread of farm to wholesale meat prices that has occurred through the same time. This clearly shows that not only does the current system not help independent beef producers but it also does not help the American consumer either.

We are asking the Kansas legislature to enact a ban on packer ownership. I am sure that you are thinking that this should be a national issue and not a state law. Yes you are right, however too often, federal policy shifts have to be directed by state mandates. We in the individual states need to show leadership to congress in what needs to be done in the livestock industry. There are good examples of states that have already made state changes addressing this issue, Nebraska, Iowa, Minnesota, and South Dakota. As strong as the livestock industry is here, Kansas would really show leadership by enacting an effective ban on packer ownership.

Thank you for your time.

House Agriculture Committee  
February 24, 2003  
Attachment 2

Testimony of Malcolm Moore, R-CALF Director, Region #6

My name is Malcolm Moore. My family and I raise cattle in Shawnee County. I am the R-CALF Director for a six state area which includes Kansas. R-CALF is the fastest growing cattle group in the world. In four years we have grown to over 8,000 members in 43 states. R-CALF is concerned with trade and marketing issues only. We worked with other groups to pass COOL Country of Origin Labeling.

The U.S. Senate also passed a ban on packer ownership that was stripped in conference committee last year. 5 other states currently have bans on packer ownership. Kansas needs to be one of these states. We need to let our Representatives and Senator in Washington know this is an important issue since neither of our Senators voted for the ban when it passed the full Senate.

Free trade has taken its toll on Kansas and other farm states. The only people who benefit from free trade are Con-Agra, Cargill, ADM, and Monsanto. These companies spend millions of dollars on public relations to convince the public, our universities, and our farm organizations that they are benevolent corporations that only have our best interest in mind. They restore saltwater swamps and feed a hungry world. They don't tell you they are relieving the State of Kansas of its valuable resources such as draining the Ogallah Aquifer and breaking our local economies.

The time is now. Either choose between the profits of the corporations or the life of our state. A ban on packer ownership bill is just a small step toward restoring our markets.

**House Agriculture Committee  
Testimony by Mike Schultz  
Executive Director  
Kansas Cattlemen's Association  
February 24, 2003  
House Bill #2167**

Mr. Chairman and members of the committee,

My name is Mike Schultz. I am from Brewster, Kansas. I am actively involved in every aspect of the farming and cattle industry in that my own operation is a farm and ranch, including a 150 cow/calf operation (with exception to the current drought sell-off). I am a very diversified business owner with a licensed commercial and residential plumbing business, rural trash service and I am a full time City Superintendent. My livelihood is dependent on production agriculture and area citizens in our surrounding rural communities.

Today I come before you as the Kansas Cattlemen's Association (KCA) Executive Director. I am representing about **1500 independently paid members** in our grassroots producer organization. We are the fastest growing cattle organization in Kansas. Last year alone we saw a 65% growth in new membership. We have gained respect from producers because we work for producers. We also now have several feedyards and independent feedyard managers working with us in a Support Program. The number of cattle we represent would be a number of significant proportion to other organizations across the U.S.

I have been here before testifying on a similar bill back in February of 2001. Today House Bill #2167 that you are hearing testimony on, would protect producers from what continues to happen to them by the market power of the meat packing industry.

I have included in your packet two handouts for reference and legal clarification. The **Beef Study** was provided by an independent research firm. The study provides support on the issue we are discussing today. It is a valid study in the fact that it received a 40% response. Why a **Beef Study**? First, it had not been done. Second we wanted to know if producers and consumers supported the same issues that KCA supported and has worked for. The methodology of the study is included and that it went to people with incomes of or exceeding \$100,000.00 from beef production.

**I want to stress to everyone here today that in this study is a solid representation of the industry that when asked about whether meat packers should be allowed to own, feed and finance their own cattle for their own plants, 92% said NO they should not be in the business to: OWN, FEED OR FINANCE THEIR OWN CATTLE FOR THEIR OWN PLANTS!** Remember this response is from those you are representing as legislators.

The other article is from Drake Journal of Agriculture Law was written by leading agricultural lawyers, Associate Professor Dr. Roger McEowen from Kansas State University, Dr. Peter Carstensen from the University of Wisconsin and Dr. Neil Harl from the University of Iowa. In the article are the reasons we are here today. What are the conditions in the market that have made legislation possible? The reasons for legislation are: consolidation amongst firms in the meatpacking industry, implications of the diminished cash market for hogs and cattle in recent years due to packer-owned and contracted livestock, and the inability or unwillingness of government enforcement agencies to address the problems. Nebraska, Iowa, Minnesota and South Dakota already have similar legislation in place. The "dire" consequences the economist have predicted has not happened in the livestock sectors with comparable legislation.

To further point out that under this legislation it does not effect marketing contracts, this bill narrowly targets contracts where a base price is negotiated before slaughter. Please understand that: **The point in this bill is to prevent packers from using contracted livestock to manipulate the cash market. The motive for strategic behavior by dominant firms in the hog and cattle sectors is further increased by the fact that the cash market is the primary price discovery point for formula contracts and marketing agreements. Thus if the cash market declines, packers pay less for livestock whether procured through the cash market or contract. Furthermore, we should keep packers from establishing a base price in the cash market in which the packer is an active buyer or a base price that is tied to a plant average price paid for the week before delivery. The packer in these conditions can still manipulate the market.**

Remember some of the findings during the R-CALF trade investigation in 1998 with United States International Trade Commission or USITC.

Commissioner Thelma J. Askey stated: "My review of the record indicates that the comparative difference between the levels of concentration in the beef packing industry and the feedlot operators leads to unequal bargaining positions between the two groups. **This disparity in bargaining positions enables to beef packers to influence price levels in the slaughter market to a significant degree.** Accordingly, the feedlot industry are price takers in the market, due to the level of concentration in the beef packing industry and the diffuse nature of the cattle industry".

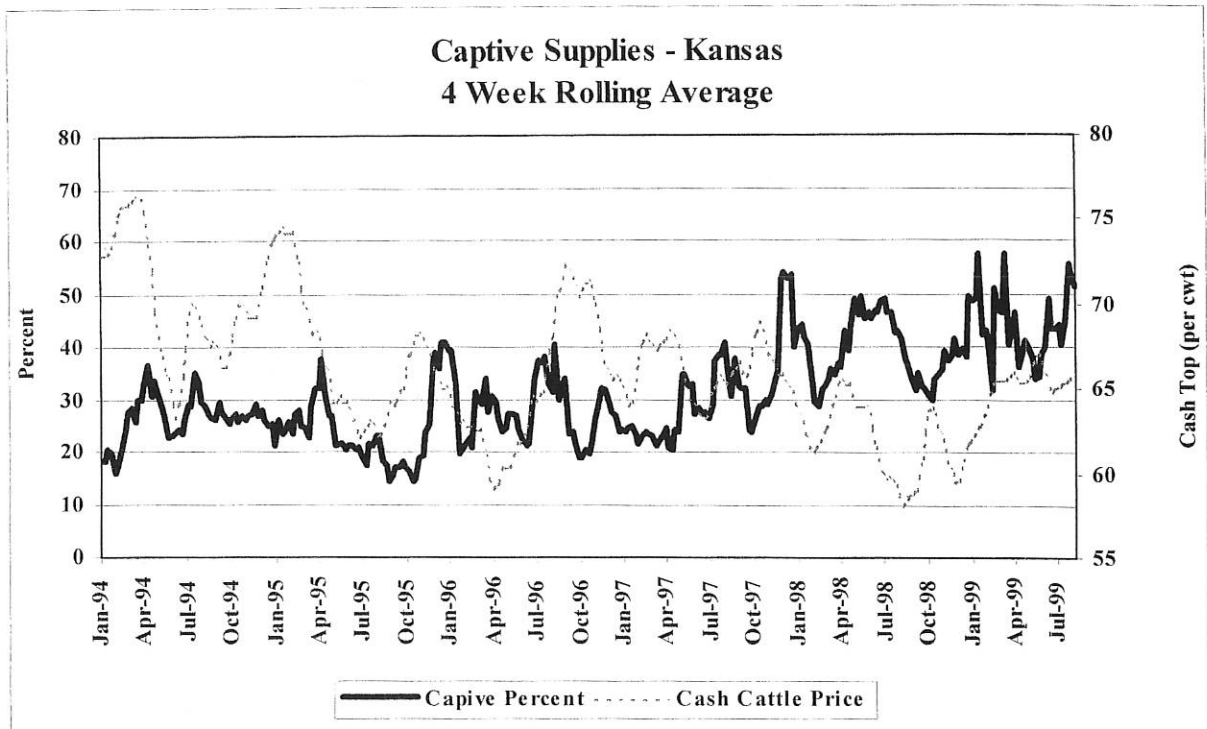
The cash cattle market is supply sensitive. When packers have captive supplies as KCA has shown, they do force the cash market lower. (See the charts below) This is a very corrupt and abusive form of the packer market control.

We ask that you take a leadership role, give approval to this bill to be heard by the entire legislative body, then send a message to Senator Pat Roberts, Senator Sam Brownback and Representative Jerry Moran to give support to Senator Grassley's Senate Bill # 27.

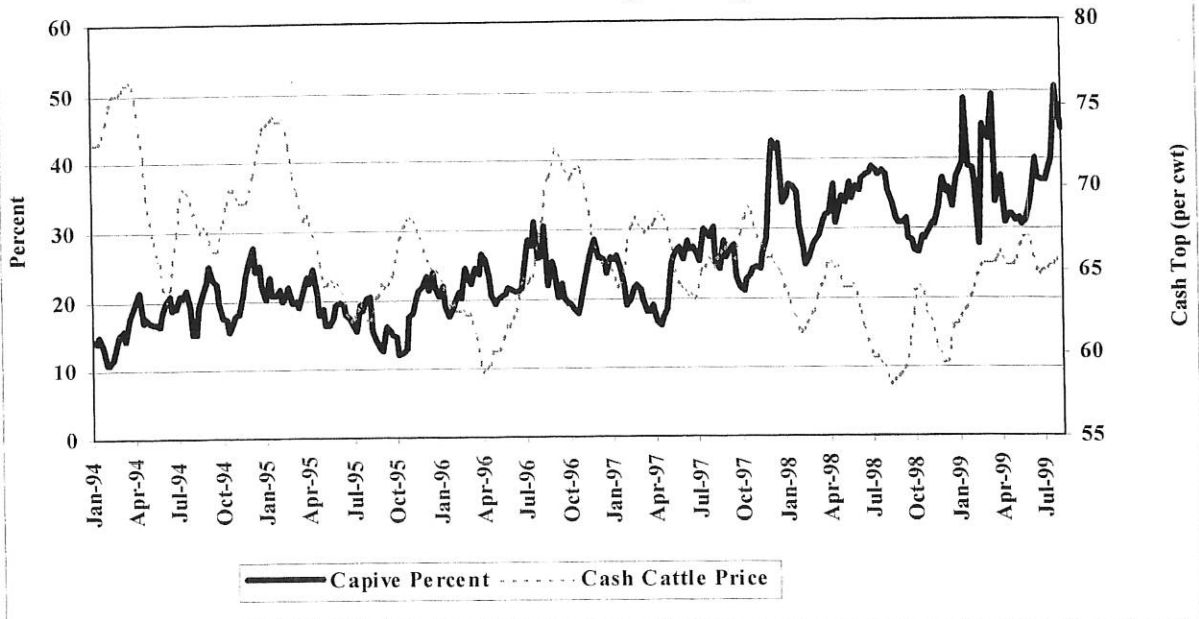
It is time for legislators together to put strict enforcement into the laws, return profit back into rural Kansas and for rebuilding a competitive market and fairness for all cattle producers. The passage of this bill will do just that. **We will not build a so-called wall around Kansas, but will restore a competitive and fair marketing system benefiting all producers.** Please consider all of the information. We ask for your support on House Bill #2167. I now stand for questions.

Respectfully submitted,

Mike Schultz  
 Executive Director  
 Kansas Cattlemen's Association  
 877-694-2906



### Captive Supplies - Total 4 Week Rolling Average





# Beef Industry

## *Producer's Questionnaire*

July 29, 2002

*Presented by:*

**RJW Research Partners**  
Dodge City, KS 67801



PO Box 251  
Brewster, Kansas 67732  
(877) 694-2906

# Beef Industry

## *Producer's Questionnaire*

### METHODOLOGY

The objective of this survey was to determine a “general” feeling among beef producers about certain beef industry developments—specifically, involvement of the packing industry in beef production and cattle numbers.

During the month of June, 2002, 1,250 questionnaires were mailed to a select target audience of what the agricultural research industry terms Class IA producers, or those with income from beef production at \$100,000 or above. The list was purchased from *High Plains Journal*, using a random selection (nth names) of the target audience. *High Plains Journal* has a high quality list, due to being an entirely paid subscription publication.

As a result of the list quality, only .32% or four questionnaires were returned as undeliverable mail needing address correction.

Mailings included a single-page questionnaire, a stamped, self-addressed postage-paid envelope, a cover letter and a one-dollar bill incentive. Copies are included in the appendix of this report.

A total of 497 or 39.9% of the questionnaires were returned. None were disqualified as all had been answered correctly. Each question was answered by all 497.

Four quantifiable questions were asked, each based on a three-point ordinal scale of strongly agree, agree and strongly disagree. Some questions were multi-part, asking specific responses to sub-categories within the question.

Following is a question-by-question summary of the results.

## EXECUTIVE SUMMARY

An overall look at the answers shows that beef producers have some definite ideas about how packers are affecting the market but they are unsure how this move has affected some specific aspects.

For instance, 90% believe that consolidations and mergers have eliminated competition; but when you conversely (as a safety check to asking the same question twice) ask them if it has helped increase competition, 24% are undecided. Also, 25% are undecided that mergers and consolidations may have helped raise prices. But a whopping 65% are unsure that the mergers and consolidations may have lowered prices.

On the marketing side, an overwhelming number believe that mergers and consolidations have affected cattle marketing in some way. Also, 97% agree that country-of-origin labeling should be done; 91% say it is an important thing to do as a way of educating consumers. A total of 95% of respondents believe all meat coming from outside the USA should be subject to the same inspections as domestic beef.

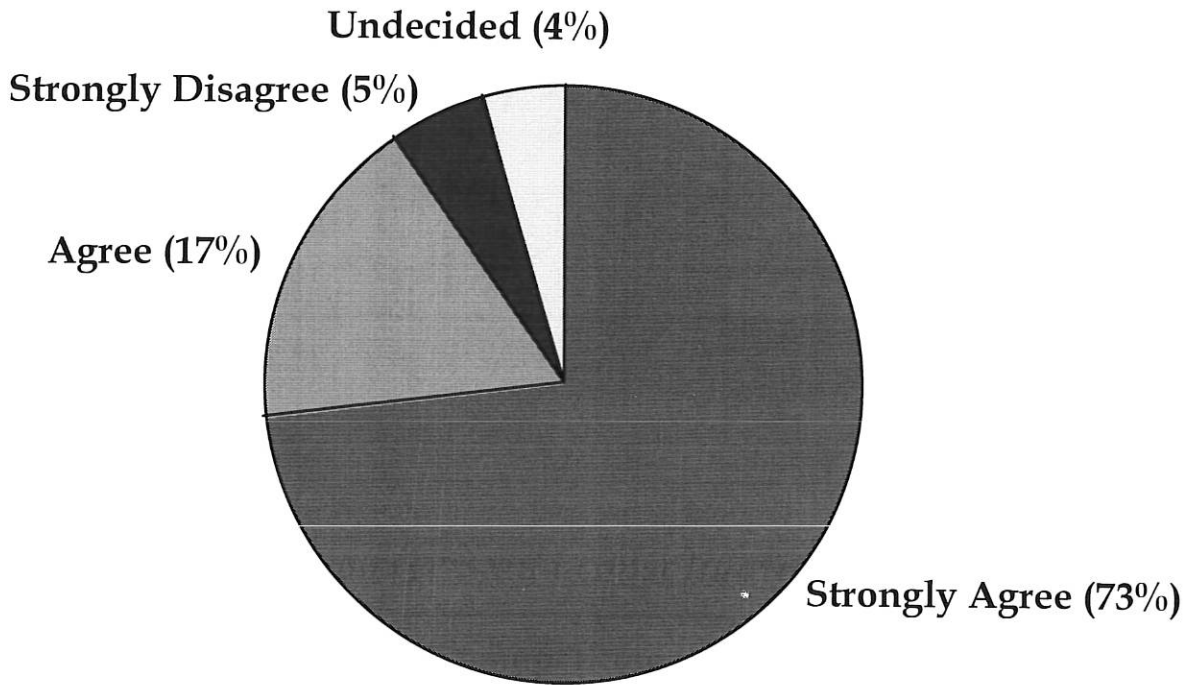
When asked about whether meat packers should be allowed to own, feed and finance their own cattle for their own plants, 92% said no.

And when asked if the USA raises enough cattle to supply domestic consumption, 93% said yes.

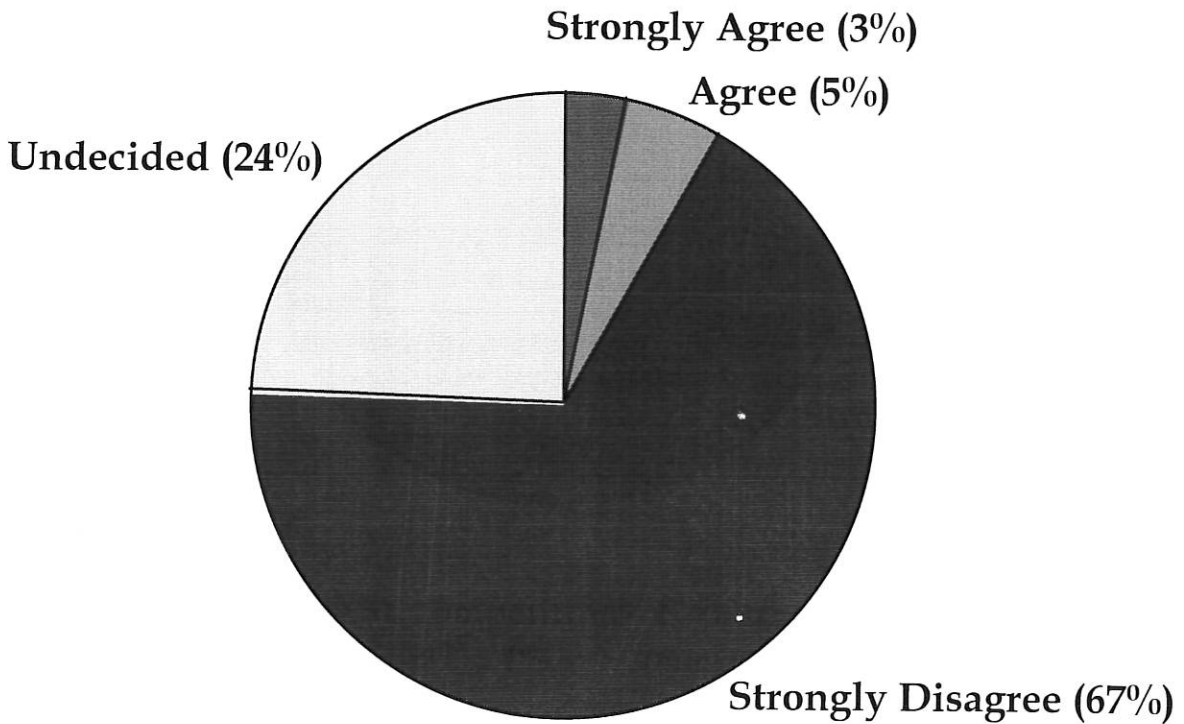
Recommendations? Clearly, there is a need for research to clear up some questions about how mergers and consolidations have affected the market, particularly with regard to prices. But there seems to be no question in producers' minds that packers should not be allowed to own, feed and finance their own cattle for slaughter.

1. *Overall I feel that mergers and consolidations in the beef industry:*

1a. **ELIMINATE** competition – *73% strongly agree*

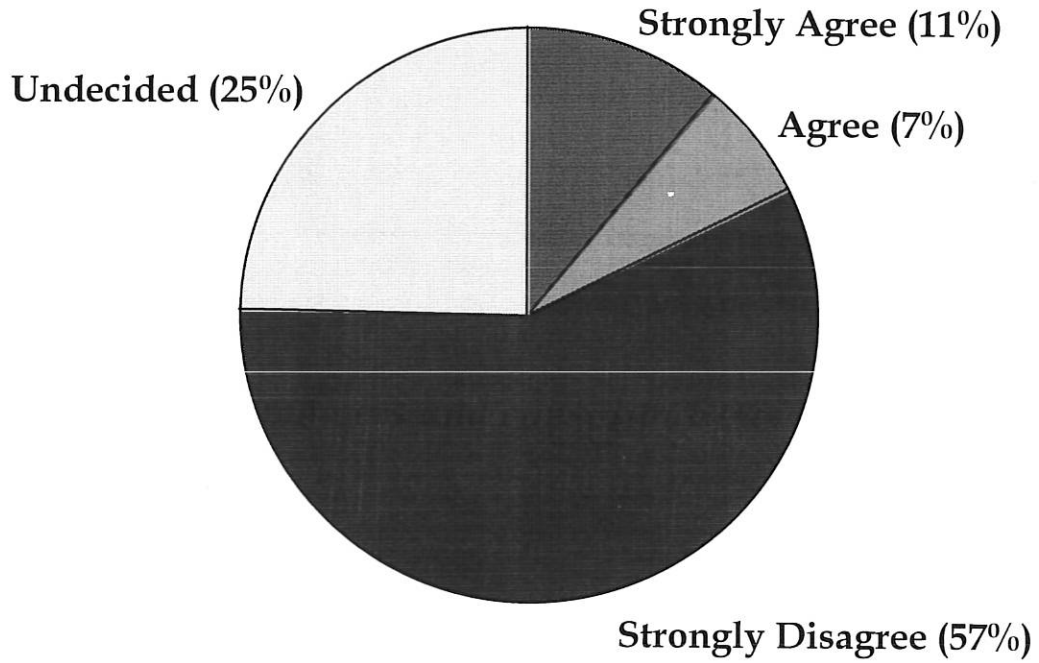


1b. **INCREASE** competition – *67% strongly disagree*  
*(BUT, 24%, are undecided)*

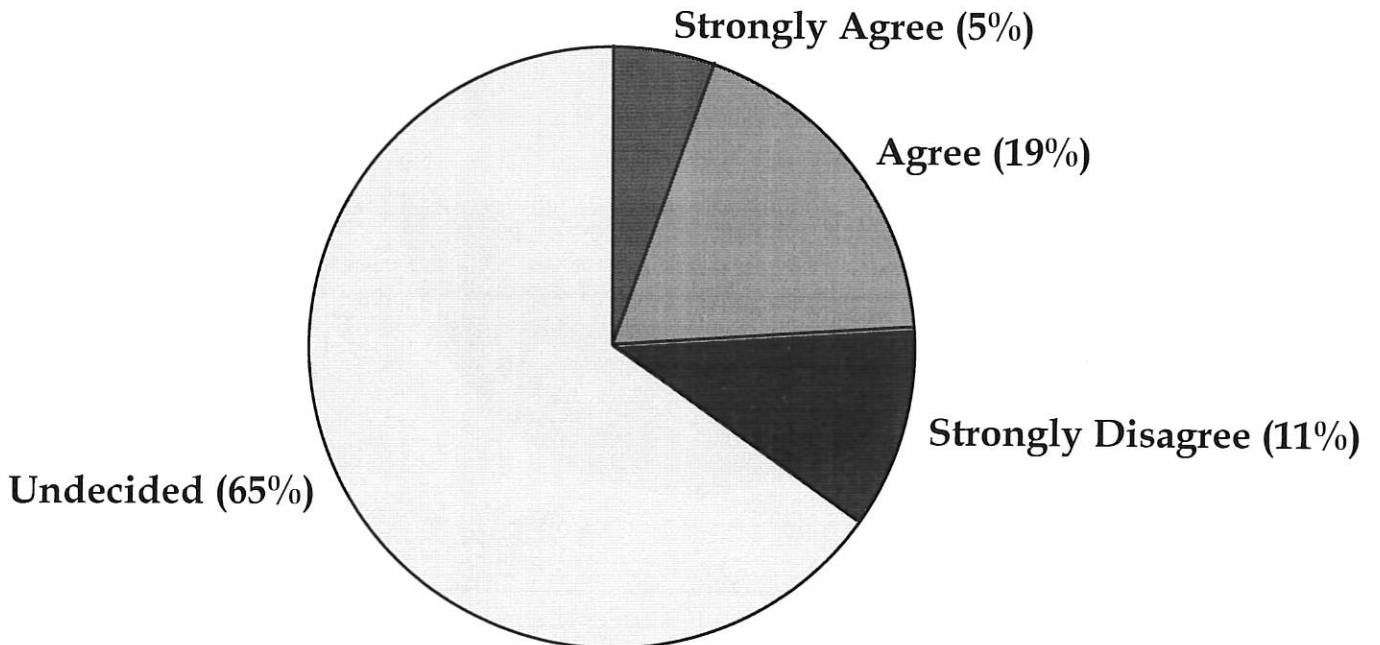


1. :Overall I feel that mergers and consolidations in the beef industry:  
(continued)

1c. RAISE prices – 57% strongly disagree  
(a large portion, 25%, are undecided)

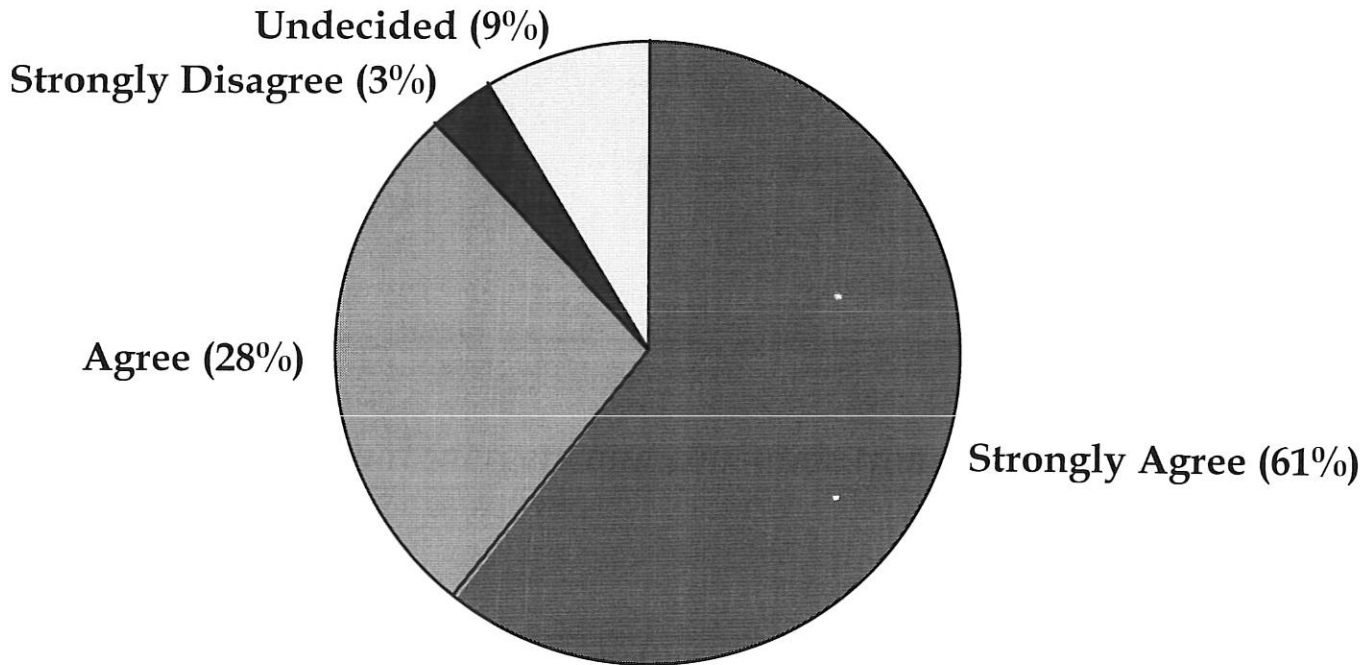


1d. LOWER prices – 65% are undecided



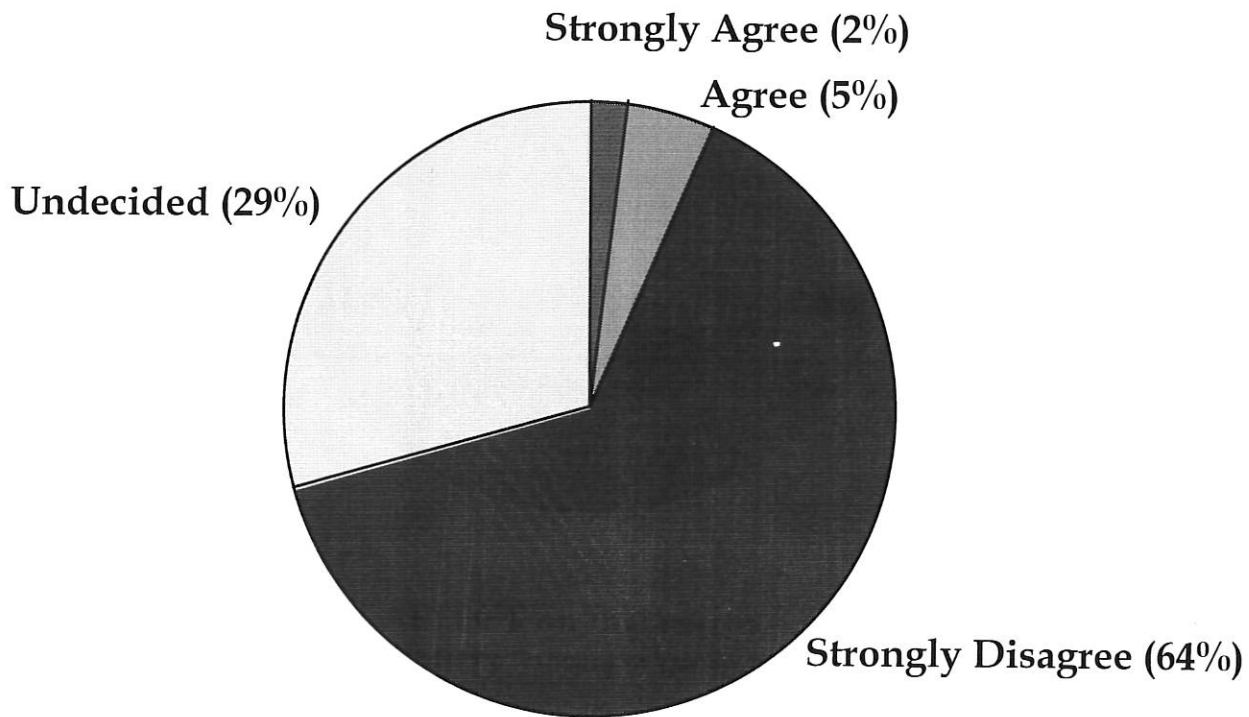
1. :Overall I feel that mergers and consolidations in the beef industry:  
(continued)

1d. AFFECT marketing – 61% strongly agree



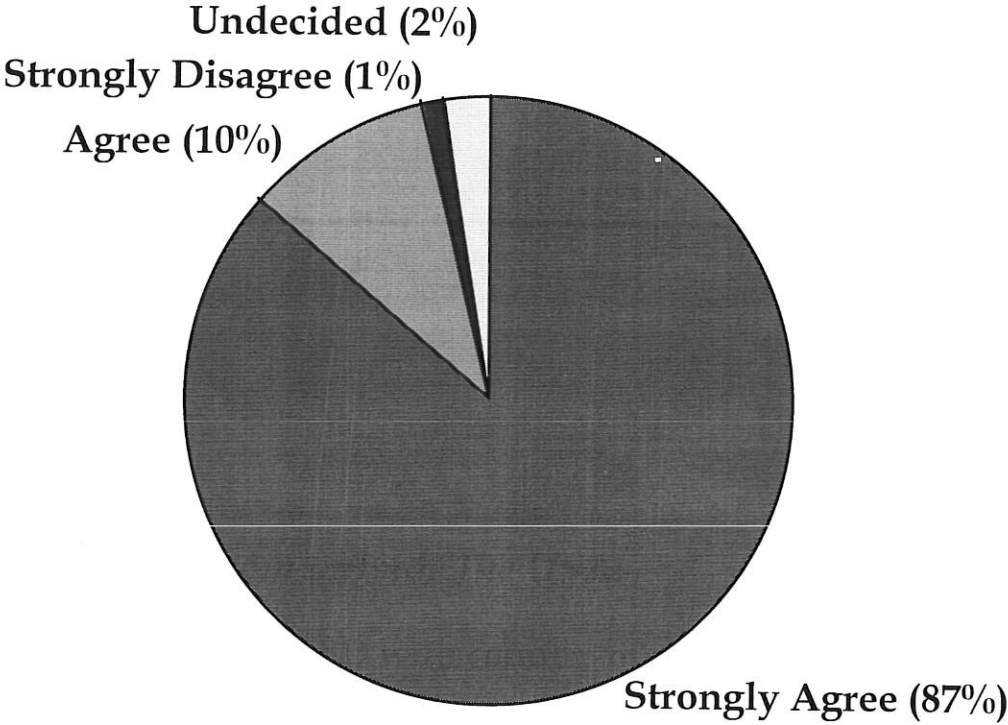
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1e. Have LITTLE AFFECT on marketing – 64% strongly disagree  
(BUT 29% are undecided)



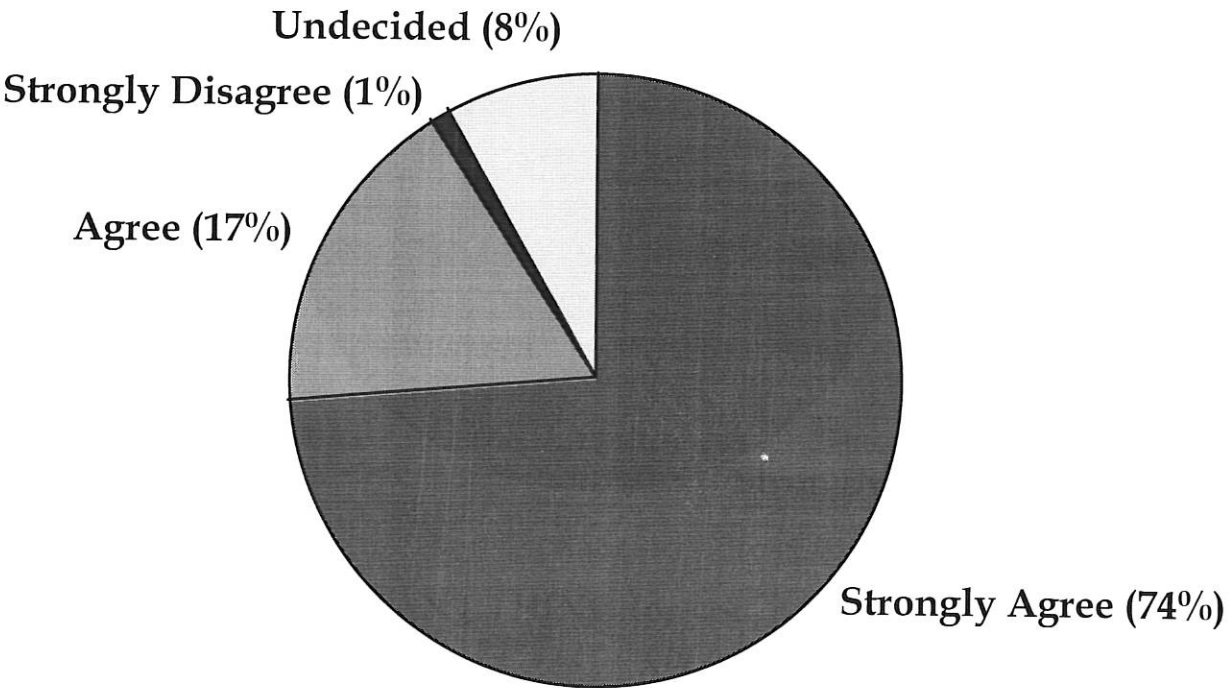
2. All meat coming from outside the USA:

2a. SHOULD BE LABELED with country of origin – 87% strongly agree



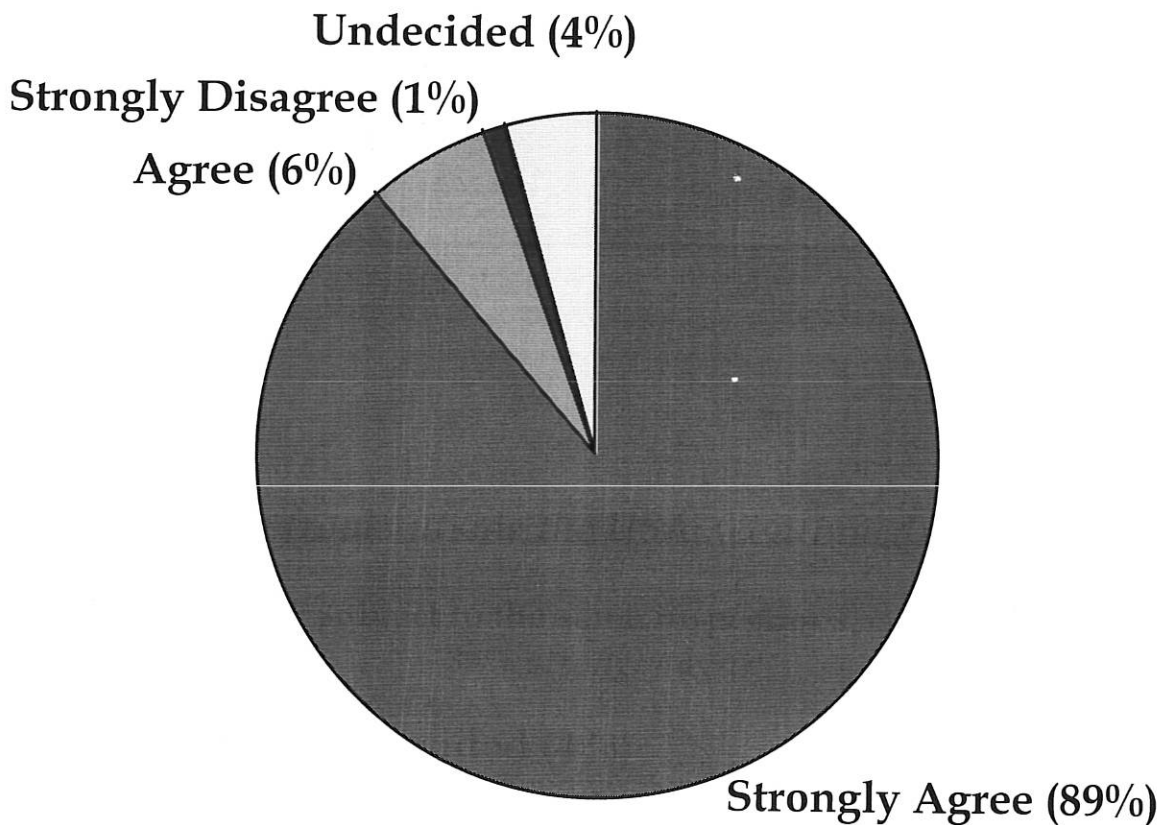
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2b. IS AN IMPORTANT THING for you, as a consumer, to know – 74% strongly agree



2. *All meat coming from outside the USA: (continued)*

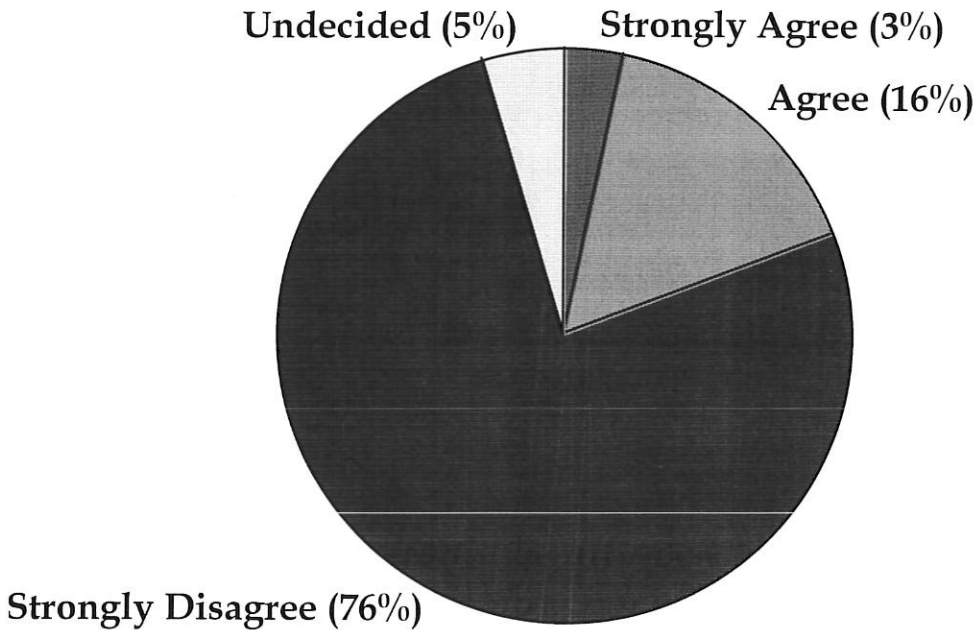
2c. SHOULD BE subject to the same inspections as domestic beef  
– 89% strongly agree





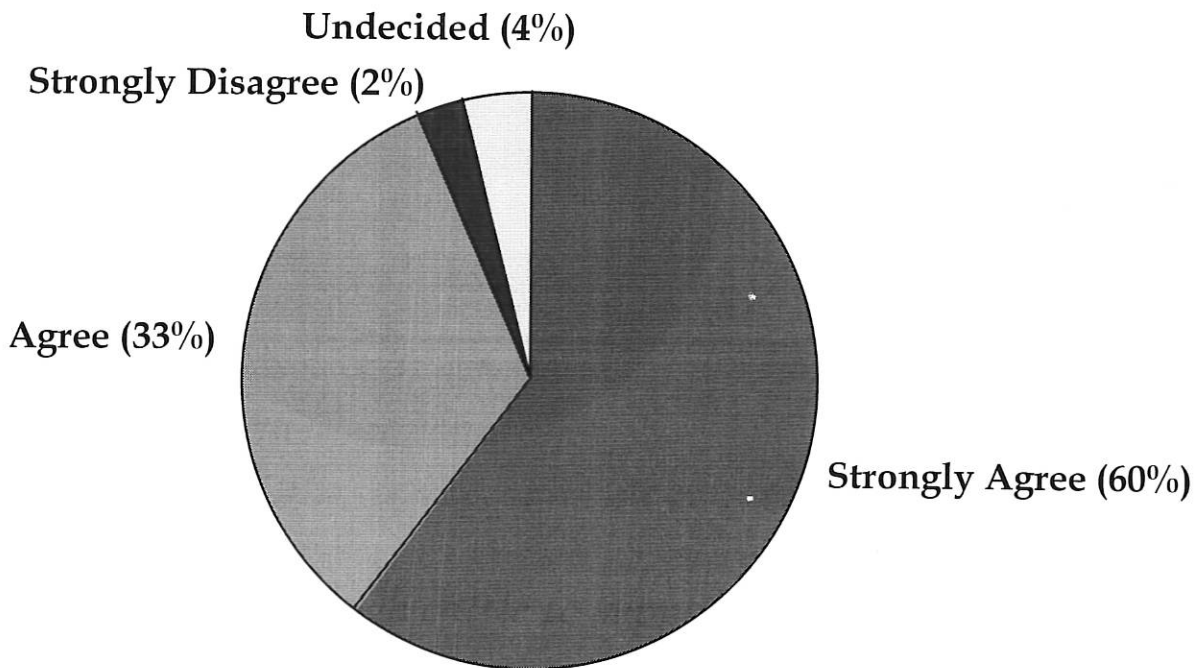
3. *Meat packers should be allowed to own, feed, finance livestock to be slaughtered in their own packing plants.*

*– 76% strongly disagree*



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4. *The USA raises enough cattle to supply domestic consumption – 60% strongly agree.*



5. *What is your number one concern for the beef cattle industry? (samples of selected comments)*

1. There is not a lot of profit for farmer feeders, and packers should not be allowed to finish cattle.
2. The KLA needs to be more in tune with the producers and get a clue about the real day to day problems.
3. Slow down or stop the consolidations. Put stricter regulations on imports.
4. Make imports be graded the same way U.S. Beef is graded.
5. Lack of profitability of fat cattle operations.
6. Consolidation of feed lots and feed companies.
7. The packing company becoming monopolized.
8. Packer ownership has affected marketing to an extent that the packers appear to be the only ones showing profit. Why are we importing beef, it is ridiculous.
9. Get packers back to "packing" or we will soon go the way of the chicken.
10. There is too much difference in the price that the farmer gets paid and what the consumer pays.
11. KLA has not been working with feed lots, but they have been working with packers.
12. Packer concentration and ownership of cattle by packers more than 96 hours prior to slaughter.
13. Market manipulation. The FMD test making news in April to up the market and then they found a woman with CJD disease. Organizations like PETA giving inappropriate information to media and info groups.
14. Local businesses buying beef outside the USA, McDonalds.
15. Big guys trying to force out the small boys just like in the hog industry.
16. Keeping the independent cow-calf operator profitable, without being dependent of government subsidies.
17. That as producers we have lost control of our product.
18. Disease and bioterrorism.
19. Change "Eat Beef" to "Eat American Beef" and stop all beef imports.
20. The consolidation of the meat packers and the integration of the whole beef industry.
21. Trade of the CME futures by people who have nothing to do with the cattle industry.
22. Ability to market cattle direct from the farm and not getting a fair share of the consumers dollar.
23. Letting meat packers own, feed, and finance livestock to be slaughtered will hurt the beef industry.
24. The new TB testing and the cost for Texas producers as a result of Mexico importing to the US.
25. Captive Supply
26. Unprofitability for the producer because of captive supplies, vertical integration, and consolidation of packing and retail segments. The disappointment that the KLA and NBCA are unwilling to do anything about it.
27. To not get Mad Cow.
28. Imported cattle being branded US beef.
29. Reduced competition to purchase fat cattle. Increased pressure from reduced consumer demand compelled with increase domestic production and increased imports.
30. Keeping market prices high enough so the rancher can come out ahead at the sale.
31. Lack of overall quality of beef.
32. That the consolidation of giants will eventually cut out the little producers all together.
33. Get rid of the futures. More money goes east than comes west.

34. Need more representation in Washington, DC.
35. The cattle industry will be controlled by few people.
36. Survival
37. The market is sometime so marginal that the difference in making a profit and losing is not appealing to the youth that the are forced into looking elsewhere for a career that is off the farm.
38. Packers not aging the beef so consumers don't get quality beef.
39. Check off is used against the producers.
40. Not if we get BSE & foot and mouth in this country, but when because of word trading.
41. Feel undercut by government because of allowing imports.
42. I am afraid you have waited to long as we are all about broke.
43. First check off is wasted on Hollywood actors. It is also to much, maybe \$.25 would be better.
44. Lack of competition.
45. That every disgruntled seed stock producer, stocker, cow calf operator, and feeder would join and already established organization at both state and national levels. Stop bickering between livestock groups.
46. The whole future of the industry depends on if we become more united.
47. Lack of good prices and drought conditions.
48. Cost of operating and inheritance tax.
49. USDA
50. The bottom is about to fall out and we will never recover.
51. To few companies with too much financial and political power.
52. Need for consumers to know where their beef is coming from.
53. Spread of Chronic Waste Disease from elk and deer to cattle.
54. Not to go the same way as the hog and chicken.
55. Different breeds preceeded difference-Holestine, for example, because of the meat market there is no different price.
56. Secure safe consumption, stabilize price, and stewardship practice.
57. Rumor affecting the market every day.
58. NAFTA ruining the industry.
59. Cattleman independence.
60. Captive Supply.



June 21, 2002

**Dear Beef Cattle Industry Producer:**

We need your help!

The *Kansas Cattlemen's Association* would like to find out how you feel about developments in the cattle industry. They've asked us here at High Plains Advertising Agency to ask you a few questions.

We've enclosed a very short anonymous one-page questionnaire to tell us what you think.

Please accept the attached token of our appreciation for your help.

And be sure to use the enclosed, self-addressed, stamped envelope to send us your response. If you wish, you may fax us your questionnaire at 620-227-7173.

Thanks so much for your help!

Most sincerely,

**HIGH PLAINS ADVERTISING AGENCY**

P.S. — Be sure to tell us what you really think. Remember, the survey is anonymous.

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1500 E. Wyatt Earp Blvd. • P.O. Box 760  
Dodge City, KS 67801-0760

4-16

# Beef Industry

## Producer's Questionnaire

*The Kansas Cattlemen's Association needs your help!  
We would like your input about beef industry developments.*

1. *Overall, I feel that mergers and consolidations in the beef industry:  
(check all that apply)*

	strongly agree	agree	strongly disagree
Eliminate competition	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Increase competition	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Raise prices	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Lower prices	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Affect marketing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Have little effect	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

2. *All meat coming from outside the USA:*

	strongly agree	agree	strongly disagree
Should be labeled with country of origin.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Is an important thing for you, as a consumer, to know.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Should be subject to same inspections as domestic beef.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

3. *Meat packers should be allowed to own, feed, finance livestock to be slaughtered in their own packing plants.*

	strongly agree	agree	strongly disagree
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

4. *The USA raises enough cattle to supply domestic consumption.*

	strongly agree	agree	strongly disagree
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

5. *What is your number one concern for the beef cattle industry?  
(use back if you wish)*

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**Thank you!**

Your help is greatly appreciated! Please return to *High Plains Advertising Agency* in the enclosed, self-addressed, stamped envelope. Or fax to 620-227-7173

House Ag Committee

Testimony by David Pfrang

February 24, 2003

HB 2167

Mr. Chairman and members of the committee,

My name is David Pfrang. I am an independent cattle producer from Goff, KS, in Nemaha County. I'm one of the very few remaining producers who raise cattle from start to finish at home.

Cattle producers depend on an open, competitive market for their income. They do not rely on government price supports. Independent cattle producers determine the terms of their production, the terms of their marketing, and they allow competition to determine the value of their livestock. Maintaining a competitive marketplace is, therefore, the principle objective of independent cattle producers.

Independent producers defined the legal framework of their markets in the Packers and Stockyard Act of 1921. Within this Act, rules were established to ensure that dominant parties within the beef industry could not interfere with the competitive forces in the marketplace.

Packers use packer-owned cattle to manage their per unit costs. R-CALF USA believes that the practice of using packer-owned cattle to manage per unit costs means that they are controlling cattle prices, and this is a violation of the Packers and Stockyards Act. However, the Packers and Stockyards Administration has made no attempt to enforce the Act with respect to packer-owned cattle.

How do we know packers are using packer-owned cattle to control cattle prices? When packers own and feed their own cattle, they eliminate one of the three competitive arenas that, together, function to foster a competitive marketplace for the live cattle industry. They are effectively eliminating the competition between the feeding sector and the packing sector of our industry, thus shrinking the number of buyers available for the backgrounder to feeder markets and the producer to backgrounder markets.

Banning packer ownership of livestock will not eliminate all the marketplace control exerted by packers. There are other tools that packers use to interfere with the competitive marketplace to manage their per unit costs. In addition, packers have introduced new cattle procurement tools that afford them

control over livestock without having to establish a price for the cattle. These tools include formula and grid pricing, non-priced forward contracts and marketing agreements. Cattle committed to packers using these tools are captive supply cattle and have the same affect on the market as packer owned cattle. Furthermore, access to ever-increasing supplies of both imported live cattle and imported beef afford packers with market leverage similar to captive supplies.

The ban on packer ownership will not address the entire problem, but it will have the greatest impact in halting the packer's efforts to eliminate the competition between the feeding sector and the packing sector of our industry. Currently, packer-ownership of cattle is the tool used to reduce the number of independent feeders in the United States. When packers feed their own cattle, they can completely bypass independent feeders. All other forms of captive supplies (with the exception of imported cattle and beef) are acquired without shrinking the supply of feeder cattle available to independent feeders. In fact, many independent feeders are contract participants in the other forms of captive supplies. Therefore prohibiting packers from owning livestock will have an immediate dampening effect on the industry. It is the first and most important step the industry must take to restore competition to the live cattle market.

There is no greater evidence that something is wrong than to witness the record retail prices that consumers are paying and the tremendous losses that producers are experiencing.

There is no greater evidence that something is wrong than the high number of producers quitting .

There is no greater evidence that something is wrong than simply to look at the relationship between both retail and boxed beef prices and fed cattle prices.

U.S. cattle producers have become so frustrated with USDA's inaction that they are seeking relief from the judicial branch of government. I urge you to choose to promote and preserve an open and competitive marketplace, free from undue influences by the packing sector. With this choice, our independent cattle producers will be assured of both economic opportunities and choices within our free enterprise system.

Thank you for your time.

David Pfrang

WRITTEN TESTIMONY OF  
THE ORGANIZATION FOR COMPETITIVE MARKETS

KANSAS HOUSE OF REPRESENTATIVES  
HOUSE COMMITTEE ON AGRICULTURE

February 24, 2003

**HB # 2167**

**Hearing on Proposed Ban on Packer Ownership of Livestock**

Thank you Chairman Johnson and members of the House Committee on Agriculture for allowing us to submit our testimony. My name is Steve Cady and I am the Executive Director for the Organization for Competitive Markets. OCM is a multi-disciplinary non-profit organization with an exclusive focus on antitrust and competition problems and solutions in agriculture. Our members consist of farmers, ranchers, academics, policy makers and agricultural businessmen.

Our organization is a young entity, created in 1998. We work on issues of market power, market structure and market conduct.

The United States Department of Agriculture, Grain Inspectors Packers & Stockyards, P & S Section 202 states, "It shall be unlawful for any packer or swine contractor with respect to livestock, meats, meat food products, or livestock products.... to: (a) Engage in or use any unfair, unjustly discriminatory, or deceptive practice or device, or (b) Make or give any undue or unreasonable preference or advantage to any particular person or locality in any respect, or subject any particular person or locality to any undue or unreasonable prejudice or disadvantage in any respect: or...

In a speech to the Kansas Livestock Association in 1994 IBP CEO Bob Peterson said this.

First, formula doesn't imply higher than market or barter price – often quite the reverse but usually is better. Second, not formula cattle but packer-fed cattle, which can be killed early or late to fill a particular time frame, be it a day or a week, grant the packer far greater flexibility to move in and out of the market. On the way down, he kills his cattle first and on the way up, last.

I have a question. Why doesn't that bother you and formula cattle do? I don't understand. And by the way, last year when cattle brought \$85, we had about the same amount of formula cattle. Maybe that's what helped you get \$85. Maybe, just maybe.

In 1989, I told your industry right here at the KLA convention that if it allowed packers to feed their own cattle, IBP would do whatever was necessary to level the playing field. Ladies and gentlemen, the leveling is called formula and contract buying. Thus far, we have been able to partially offset the leverage our competitors have by the use of formula cattle and contract buying. Will we stop doing it? No. Will we feed cattle? If we have to. As most of you know, our recent purchase of Lakeside Farm Industries in Canada includes a feed yard.



**I am only trying to tell you one thing. IBP will do whatever is necessary to remain competitive. My Board of Directors and my stockholders expect me to act – and I will do just that. I will act accordingly.**

The first paragraph tells me that the packer is using preferential treatment in filling kill slots. The temptation to do so is very high whether they own their own cattle/hogs or they have cattle/hogs in captive supply. This activity clearly should be considered illegal under P&S Section 202.

On June 11, 2002 U S Congressman Osborne of Nebraska met with USDA Grain Inspector Packers & Stockyards (GIPSA) Administrator Donna Reifschneider and Special Counsel for Agriculture for the Department of Justice Doug Ross. Congressman Osborne sent a letter to me on 6/25/2002 in which he stated, "The agency officials with whom I met believe that their departments are enforcing the laws within their jurisdiction to the best of their current abilities."

Also producers tell me that Hormel Foods has a sign in their packing plant that offers prices to "large producers" and another standard price apparently for other than large producers. It is beyond me what the justification is for the two prices and how anyone could determine that this is just or reasonable preferential treatment!

This activity is conduct by corporations that can affect producers' profitability. In 1970 there was a legal judgment in a lawsuit called "The Bray Case".<sup>1</sup>

"The District Court, Oliver J. Carter, Chief Judge, held, inter alia, that the evidence was sufficient to authorize jury to find the defendant did conspire to effectuate beef price fixing scheme resulting in a recovery of more than \$32,700,000 in damages."

"There was sufficient evidence to support jury finding that defendant retail grocery chain, which was the largest purchaser of carcass beef in the United States and which accounted for seven to 8% of total grocery beef sale, had ability, in concert with coconspirators, to effectuate the beef price fixing plan as charged by plaintiff cattlemen."

"The jury had before it evidence that, between 1953 and 1970, the price received by the cattlemen for his cattle remained relatively constant—between 20 and 28 cents per pound. Between 1970 and 1973—a time period the conspiracy was allegedly inoperative—the price of beef skyrocketed to 43 cents per pound. The jury apparently concluded that, had the conspiracy not been in effect in 1964-1967 a similar increase of approximately 20 cents per pound would have occurred."

I mention this case because it has some very relevant points. 1) Packers today own approximately 8% of the fed cattle in the US. 2) If retailers could impact the price by 20 cents per pound it is plausible to say that packers could impact the price by 20 cents per pound. 3) We believe Bob Peterson was being very honest about lowering demand, lowering price and producer profitability by using captive supplies to control the market place.

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<sup>1</sup> 392 F.Supp.851 1975-1 Trade Cases P60,193-194, United States District Court, N.D. California Irvin BRAY v. SAFEWAY STORES, INC., No. C-48538-OJC. March 4, 1975

The US Senate passed a ban on packer ownership in the 2002 Farm Bill, which did not survive the House Senate Conference Committee. There is no doubt that livestock producers have had very low prices for a substantial period of time and that the cattle & hog price cycles are no longer working as they used to. There is a market force in place that is destroying the supply/demand signals required to maintain orderly competitive markets.

Steve Meyer, former economist for the National Pork Producers Council, in a recent paper on the cost of Country of Origin Labeling, calls the livestock markets the last and only perfect competitive market in the world. OCM considers this to be true and believes it is vital that we maintain markets that have a competitive bidding process that allows for true price discovery and price determination.

In 1996 at the South Dakota Governor's Cattlemen's Conference, Bob Peterson of IPB again spoke on packer perspectives.

**Bob's quote to producers was that "IBP is determined to get the playing field level. IBP is the middleman. You produce, we process, and they buy, the consumer. We take what it is we sell (meat) to our customers, subtract what our credits are, add back what our expenses are and bid accordingly. We're the middleman and it's been that way for thousands of years,"**

If we had truly competitive markets we would have fat cattle prices determined by supply and demand of fat cattle not by what the retailer will pay. And if we had truly competitive markets we would have prices determined in a bid and offer environment with packers in the market every day to fill their needs.

The only true perfect market place left is the feeder cattle market which is a bid and ask, supply and demand driven price discovery vehicle (auction market). In 1960 almost all livestock was sold on the open market either in auction markets or terminal markets. Today almost all "Harvest Ready" livestock is sold direct to the packer without true price discovery.

I have attached a copy the United States Senate Committee on Agriculture, Nutrition and Forestry Hearing on Proposed Ban on Packer Ownership of Livestock and USDA's Enforcement of the Packers and Stockyards Act testimony for the Organization for Competitive Markets presented by our Legal Counsel, Michael Stumo. I believe the testimony is enlightening and significant in its discussion of the issues faced by our US Senate in their discussions of the 2002 US Farm Bill. Your committee is trying to address many of those exact same issues. Also attached for your convenience is a copy of the Bray v. Safeway case summary.

Thank you again for allowing us to provide input to your committee on such an important issue.

Steve Cady, Executive Director

On behalf of the Organization for Competitive Markets

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Email: [skd80@diodecom.net](mailto:skd80@diodecom.net) Internet: [www.competitivemarkets.com](http://www.competitivemarkets.com)

WRITTEN TESTIMONY OF  
THE ORGANIZATION FOR COMPETITIVE MARKETS  
presented to the  
UNITED STATES SENATE  
COMMITTEE ON AGRICULTURE, NUTRITION AND FORESTRY

July 16, 2002

**Hearing on Proposed Ban on Packer Ownership of Livestock and  
USDA's Enforcement of the Packers & Stockyards Act**

Thank you Chairman Harkin and members of the Senate Committee on Agriculture, Nutrition and Forestry for allowing me to speak here today. My name is Michael Stumo and I am general counsel for the Organization for Competitive Markets. OCM is a multidisciplinary nonprofit organization that focus exclusively on antitrust and competition problems and solutions in agriculture. Our members consist of farmers, ranchers, academics, policy makers and agricultural businessmen.

The U.S. food industry grosses approximately \$900 billion in annual sales. It is the biggest industry in the country and in the world. That money is distributed through the agricultural market infrastructure. Our family farms and ranches, as well as our rural communities, were built on that money. A perfectly competitive market would distribute that money properly. A noncompetitive market does not allow that money to flow to rural communities. Rather, dominant firms utilize their position to obstruct that monetary flow and enrich themselves far beyond the level that could otherwise be achieved without near-monopoly power. The result is an increasing rate of farm failure, increased consumer food prices, and harm to the public interest.

**I. The Nature of Agricultural Markets and the Need for Market Facilitating Rules**

The role of government in the marketplace is to create and maintain the infrastructure for the most people and companies to engage in commerce. The analogies are the internet and the U.S. interstate highway system. The internet is not commerce or communication. Rather, it is an infrastructure that facilitates cheap and effective commerce and communication. It is not proprietary. It is accessible by most everyone, and it is very easy to access.

Similarly, the U.S. interstate highway system is not commerce. It facilitates commerce. Everyone can use it. There are many on ramps and off ramps. General Electric uses the system and so does my mother. The government maintains it and applies a set of equitable rules to the infrastructure. The payback has been incredible.

It may be efficient for four companies to acquire exclusive use of 50% of the internet or 90% interstate highway system. But it is efficient only for the companies' profitability. It is not beneficial for the country because it denies the benefits of commerce and communication to the displaced users.

The livestock marketplace must be similarly open, accessible and fair to benefit the broadest number of people. We must have rules that maintain access by all through many on-ramps and off-ramps. We must maintain inexpensive use by all under equitable terms. If a company feels it would be more efficient to exclude others from the system, that desire must be recognized as in conflict with the public welfare. We must maintain the ability for the broadest participation in commerce possible for widespread rural economic health.

Federal policy applied to the stock markets has promoted fairness, access, transparency and competition in the stock markets. The result is that 80 million people own stock, a far larger percentage of the population than of any other country, and those people can make trades easily and cheaply. Federal policy applied to the livestock markets has promoted unfairness, market closure, secrecy, and monopolistic practices.

We need to rethink the emphasis on efficiency in macro-market policy. "Efficiency" is relevant to a firm producing more for less money, but it is far less relevant to proper market operation. Stated another way, if efficiency gains occur, a competitive market will distribute those efficiency gains to society. In a non-competitive market, the efficiency gains are not distributed.

The analysis relating to market facilitation and efficiency should be as follows: First, the focus should be on creating a market system that is fair, accessible, transparent and competitive. The internal logic here is separate from efficiency. Second, if efficiency is raised as a negative factor, the following four questions must be asked before balancing the efficiency argument with the anticipated market facilitation effects: (1) Are the claimed efficiency gains/harm real? (2) Are the efficiency gains directly related to the market practice at issue? (3) Is there no other way to achieve the claimed efficiency gains? (4) Are the efficiency gains likely to be passed on to consumers or farmers, or is market power likely to obstruct passing the gains on to others. If the efficiency gains are real, related to the practice at issue, achievable in no other way, and likely to be passed on to consumers/producers, then we can quantify what efficiency gains are relevant and weigh them against the positive effect of the market facilitating rules contemplated.

#### **A. Captive Supplies: The Problems**

Captive supplies of livestock are all livestock committed to packers through packer ownership and contracts more than seven days prior to slaughter.<sup>1</sup> The fundamental market problems of captive supplies are threefold: (1) market closure; (2) market unfairness; and (3) enabling packers to "game the system" just as Enron and Dynegy gamed the energy trading system.

##### **1. Market closure**

Captive supplies have progressed to the point where hog farmers cannot get bids or access to markets, even in states with large packing capacity, such as Iowa, Nebraska and Minnesota.

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<sup>1</sup> The industry, specifically most cattlemen's associations that have addressed the issue, uses the seven day rule. However, USDA-GIPSA uses a 14 day prior-to-slaughter rule. See, USDA GIPSA publication, "Captive Supply of Cattle and GIPSA's Reporting of Captive Supply," released January 18, 2002 (on the web at [www.usda.gov/gipsa/pubs/captive\\_supply/captive.htm](http://www.usda.gov/gipsa/pubs/captive_supply/captive.htm)).

Pork packers own 20 percent to 25 percent of the hogs they slaughter. That is 77,000 packer owned hogs per day at 22%. That is over 20 million hogs per year that displace family farm produced hogs. This, at its core, dampens or excludes widespread rural commerce. If we like a diverse and decentralized production system, we are not promoting it.

But what of the remaining "open market" participants? We know that about 16% of each day's slaughter is claimed to be open market, using USDA daily market news reports.<sup>2</sup> No one disagrees that farmers have difficulty accessing the market. But what is not widely known is that most farmers who seek bids on their hogs no longer get bids, even in Iowa which has more pork slaughter capacity than any other state. Rather, they get "slots" or "shackle space" at some time in the next seven to fourteen days. The packer tells the farmer what the price is after the hogs are delivered. That price is reported to USDA Market News Service. No bids. No competition. That is our dysfunctional open market price discovery system. We are losing much decentralized economic activity in the form of broad family farm market participation.

## 2. Market unfairness

To the extent participation is allowed in the markets, participants are treated unequally. Large corporate producers receive preferential contracts. For example, the large feedyards owned by Sparks, called Cattle Co., appear to have contracts with packers which allow significant price advantages over other producers of cattle. It is undisputed that producers are treated disparately with regard to contract offerings, bids, and access. But it is disputed whether these practices are legitimate. If we apply basic and successful market principals to our evaluation of these activities, the answer is clear that disparate treatment is contrary to proper market operation and contrary to the public interest.

If a small farmer produces high quality hogs, he/she should get access to prices and shackle space according to quality, not quantity. If a large farmer produces high quality hogs, the same result. Size is not relevant to hog quality. Further, the transaction costs arising from purchasing from many producers, rather than a few large producers, is so small as to be insignificant. The primary goal should be fairness and access to facilitate widespread and decentralized rural commerce.

A properly functioning free market provides uniform rules for all participants on price, premiums, discounts and access. The stock market does so. Warren Buffet gets no better terms than Michael Stumo when buying stock at a particular time – even if he buys 500,000 shares of GE when I buy 50 shares. Buffet may analyze information and have better strategies to time his purchases and sales, but we have equal market access at the same price on any given time and date of trading. The same should be true in the livestock markets.

The Packers & Stockyards Act should be to "live-stock" what the Securities and Exchanges Acts are for "paper-stock." The law is written to enable this result, but USDA has failed. More on that later.

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<sup>2</sup> This 16% contemporary figure is part of a declining trend in open market hog trading. If the current trend continues, the open market will disappear in 2004.

### 3. Manipulating or Gaming the System: The Incentive Structure

When constructing proper market rules, the proper approach is to counteract the incentives to manipulate the market or "game the system." Looking for proof of harm after-the-fact is not beneficial and this method has failed. Further, a focus on efficiency has not proven helpful and has failed.

Enron and Dynegy "gamed the system" with regard to California energy markets. They used strategies such as Death Star, Fat Boy and Get Shorty in creating fictional transactions, creating perceived shortages, and trading advantageously in the situation they created. They got wealthy, but Californians were thrown into crisis.

When undue importance is attached to a number, undue efforts are made to manipulate that number. On Wall Street, the *key number* is earnings. Shady accounting strategies are used to manipulate that number. Bernard Ebbers of WorldCom is the poster child for this scenario. But tremendous energy is expended by defenders to justify those strategies as legitimate. In the livestock markets, the *key number* is the open market price. Similarly, shady marketing strategies are used to manipulate that number. And tremendous energy is expended by defenders to justify those strategies as legitimate.

Captive supplies, such as contracted and packer owned livestock, are the raw material for market strategies equivalent to Death Star and Fat Boy. By strategically scheduling captive hogs to stay out of the market, drive the price down, and jump into the market to buy at low prices, packers make tremendous amounts of money. Farmers lose tremendous amounts of money. Yet valiant attempts are made to convince us that captive supplies are justifiable.

The fundamental principal here is that when the market is dominated by a few firms that are repeat players in a very thin market, the motive and opportunity to manipulate that thin market is so real as to be undeniable. Bob Peterson, former CEO of IBP, spoke to the Kansas Livestock Association in 1988. The following comes from the tape of his speech:

"Our competitors are promoting contracts and seeking more. These forward contracts coupled with packer feeding could represent a significant percentage of fed cattle at certain times of the year. **Do you think this has any impact on the price of the cash market? You bet! We believe a significant impact.** Large volume forward contracting and its inevitable connection to the futures trading pit in Chicago will foster severe price distortions in the cash market. In the event that contracting becomes the wave of the future, and frankly I doubt that sharp feeders will allow that to happen, IBP will be forced to respond to the competitive pressures of the market place." (emphasis added)

Even Wayne Purcell of Virginia Tech, who opposed the packer ownership ban, understands the manipulative incentives in the current system.<sup>3</sup> In testimony before USDA in Denver in September, 2000, he wrote that "[w]hether buyers attempt to manipulate the cash market to which the contract price is tied is somewhat immaterial because the incentive to do so is present

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<sup>3</sup> Purcell, Wayne D., *Contracts And Captive Supplies In Livestock: Why We Are Here, Implications, And Policy Issues*, Testimony at the Denver Captive Supply Forum, dated September 21, 2000.

and is undeniable.” It is this motive and opportunity, aka the “incentive structure,” that should govern legislative judgment to prevent manipulation.

Past USDA studies have shown a high correlation between increased captive supplies and lower prices. The most detailed study of this relationship was published in 1999, using subpoenaed packer information with the support of USDA. That study, in the beef industry, found that “a robust empirical relationship [between captive supplies and low prices] was found in every case.”<sup>4</sup> For folks who are confused, this means that when captive supplies are dumped on the market, prices drop. The economic incentive is thus shown. More captive supplies make more money for packers.

USDA explains this away saying that this correlation does not give them causation. But economists cannot achieve “causation.” Rather, a major ADM-style price fixing case with testimony, hidden cameras, and the like is necessary to give causation to the extent needed by USDA. It is time for a legislative judgment to be made.

Let us quantify the economic incentive to game the system by using captive supplies to manipulate the price through an example. If packers can use captive supply to drive down the open market price by one dollar on a day, the procurement savings is \$910,000 each day (assuming a daily hog slaughter of 350,000 head at 260 pounds per animal). That is \$910,000 taken from farmers. On an annual basis, that is \$237 million taken from farmers and transferred to packers as compared to a competitive market result. If captive supplies drive the price down by two dollars per day, we double the farmer loss and double the packer gain.

How can a dominant packer buyer game the system? The easiest way is for a packer to schedule blocks of captive supply livestock for slaughter over a period of time, pull out of the market during that time and watch the open market price fall. Then the packer can jump into the open market to buy cheaply. That cheap open market price not only saves money on the open market hogs directly, it also cheapens the tens of thousands of hogs per day that are contracted using a formula based on the open market price. If any packer buyer does not know how to do this, it is likely that any such packer buyer has moved on in his career.

Further, a packer contracts for the best hogs and, as a result, the open market becomes residual. By “residual,” it is meant that the poorer, less desirable hogs are sold on the open market. The open market price reported by USDA Market News Service is, thus, the value of the poorest quality animals. The perverse result is that the poor quality hog price becomes the base price for the hogs procured under formula-price contracts (“formula price” contracts derive the sale price based on a formula which uses the open market price as the starting point).

Additionally, the futures market relies most heavily on the open market in determining price for the future. If the open market is broken, the damage is transferred to the futures markets. In other words, the captive supplies derivatively drive down the futures market because of futures traders’ heavy reliance on open market price data.

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<sup>4</sup> John R. Schroeter and Azzedine Azzam, *Econometric Analysis of Fed Cattle Procurement in the Texas Panhandle* 46 (November 1999).

Lastly, because producers selling in the open market have no realistic bid choices, they engage in “panic selling” rather than negotiation. Certainly it is difficult to negotiate when there is only one willing buyer in the region and that buyer does not bid but merely doles out shackles with the promise of an arbitrary “price” upon delivery. The cumulative result of panic selling is not a price arising from a competitive market. From what is that post-delivery price derived from, a market? Packer gratuity? Certainly not competitive bidding.

## B. Captive Supplies: The Solutions

The only solution to captive supplies is structural, not a conduct remedy. By a “structural remedy,” I mean limiting or eliminating the partial vertical integration known as captive supplies. A “conduct remedy” means that we do not limit captive supplies but merely pass or enforce a law to prevent unlawful conduct that captive supplies could enable. Structural remedies are preferred because they do not require significant policing due to the fact that the ability to manipulate markets is taken away from dominant firms. Conduct remedies are not preferred because they require constant policing by regulators in a very intrusive way to be effective. Such constant policing has historically not been undertaken or effective.

### 1. Packer Ownership Prohibition

The packer ownership prohibition is the first step in making the markets work properly and limiting the ability of packers to game the system. This legislation would take a portion of the strategic scheduling ability away from the dominant packers and make the market more responsive to true supply and demand. It would also increase access to markets by more producers.

While some studies predicted crisis from banning packer ownership, those studies can be dismissed by one simple analysis – i.e. the historical record. The studies were not based upon the historical record, but upon wildly speculative economic projections. We know that the drastic financial losses in the industry will not occur because packer ownership prohibitions have been in effect for several years in Iowa and Nebraska. The predicted losses did not occur. Those states had, and continue to have, the largest packing capacity for hogs and cattle, respectively, in the nation. Those states have as many or more producers of hogs and cattle as any state. The strength or decline in production agriculture has not been affected in a manner more drastic than other states. Yet, the percentage of family farmers producing livestock is as high or higher than other states.<sup>5</sup>

### 2. Enzi legislation on livestock contracts

Senator Enzi has proposed a bill (S. 2021) that would require all contracts to have a fixed base price at the time of the agreement and would also require open public bidding of these contracts. This bill would transform the contract market from a secret, preferential, market harming scenario into an open market in and of itself. A contract market would still allow quality

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<sup>5</sup> See, Welch, et al., “On the effectiveness of state anti-corporate farming laws in the United States,” Food Policy 26 (2001) 543-548.



specifications and risk management. But it would severely limit the ability of packers to use contracted supplies to manipulate price.

Importantly, the Enzi bill has basic requirements for the contracts similar to the futures markets. There is a relatively small volume requirement, 40 head per contract for cattle and 30 head for hogs, that allow small producers to bid on contracts while large producers bid on more contracts. However, that legislation could be improved by adding a 14 day delivery window for each contract to limit strategic scheduling by the packer to affect the spot market price.

## II. The Regulatory and Enforcement Regime

The Packers & Stockyards Act (the Act) gives Secretary of Agriculture authority over the meat packing industry.<sup>6</sup> Unfortunately, past secretaries (or their designates) have stood before Congress stating that their authority is unclear or insufficient to encompass antitrust issues under the Packers & Stockyards Act. Those statements have been false. The Act provides the Secretary more authority over the packing industry than any other statute provides any other agency over any other industry. The Conference Report issued at the time of the Act stated that "Congress intends to exercise in the bill, the fullest control of the packers and stockyards which the Constitution permits."<sup>7</sup>

The Act prohibits unfairness, deception, price manipulation, and the creation of a monopoly, among other things.<sup>8</sup> The role of the secretary is, and has been, to undertake two categories of activities: (1) propound regulations refining the definitions of the prohibitions in the Act; and (2) enforce the Act and the regulations under the Act. Past secretaries have failed to perform these obligations. The current secretary shows no inclination to alter that trend.

### A. Rulemaking

The most inexpensive way to facilitate proper market operation, to minimize industry efforts to "game the system," and to increase fairness, access, transparency and competition is to propound regulations under the Act.

It is helpful to look to the FTC Act of 1914 as an analogy because of its similarities to the P&S Act and because of its more effective caselaw and regulatory development. The FTC Act prohibits "unfair and deceptive practices" as well as "unfair competition." The FTC has issued regulations and guidelines defining what these terms mean in the economy. The "unfair and deceptive practices" have given rise to the FTC's Consumer Protection Bureau while the "unfair competition" clause gave rise to the Competition Bureau. A similar dichotomy in the P&S Act in which the unfairness and deception clauses relate to "Producer Protection" while the price manipulation and monopoly creation prohibitions relate to competition or antitrust.

Unlike the FTC, the Secretary has failed to issue regulations or guidelines defining the key terms of the Act, including:

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<sup>6</sup> 7 U.S.C. §§181 et seq.

<sup>7</sup> Conference Report, H.R. Rep. No. 324, 67 Cong. 1<sup>st</sup> Sess., at 3 and 5-6 (1921).

<sup>8</sup> 7 U.S.C. §192.

- a. unfair practices under 7 U.S.C. 192(a);
- b. deceptive practices under 7 U.S.C. 192(a);
- c. unjustly discriminatory practices under 7 U.S.C. 192(a);
- d. undue or unreasonable preference or advantage under 7 U.S.C. 192(b);
- e. apportionment of supply that restrains commerce or creates a monopoly under 7 U.S.C. 192(c);
- f. price manipulation, control of prices or creation of a monopoly under 7 U.S.C. 192(d);
- g. conspiracies under 7 U.S.C. 192(f) and (g); and
- h. apportionment of territory, apportionment of purchases or sales, or manipulation or control of prices under conspiracy under 7 U.S.C. 192(f).

Further, the Secretary has failed to issue regulations or guidelines for other duties under the Act, including:

- a. defining unusual or suspicious marketing activity or pricing;
- b. when and how to refer violations of the Packers & Stockyards Act to the Attorney General as set forth in 7 U.S.C. §404;

This failure to refine and define the Act through regulations is at the heart of the USDA's failure to minimize unfair and deceptive practices and maximize competition. Without internal policy guidance, the USDA is limited to an ineffective "I know it when I see it approach" which gives no direction to employees investigating market activity.

Two reasons for these failures are USDA responsiveness to industry pressure and a pre-occupation with efficiency as a primary goal. USDA fails to recognize that: (a) efficiency is irrelevant to unfair or deceptive practices; (b) efficiency is irrelevant if lack of competition fails to pass efficiency gains on to producers or consumers; and (c) efficiency is a micro-concern within a firm and increasingly conflicts with competition principals.

## B. Enforcement

Even if rules are clear, intelligent and effective, they are without value unless enforcement is effective. Enforcement of the Act can come from three sources: (1) USDA-GIPSA in an administrative proceeding; (2) the Department of Justice in federal district court; and (3) private litigation. Public enforcement by USDA has failed. Public enforcement by the Department of Justice has not existed. Private enforcement has been hampered by the lack of an attorneys fees provision and a treble damages provision, both of which exist under the Sherman and Clayton Acts, to help farmers pursue remedies when they have been harmed.

What is the role of each means of enforcement? USDA and DOJ enforcement – in the best case case scenario of political will, sufficient expertise, and sufficient funding – is limited to high profile cases that set precedent. Government enforcement cannot hope to be the primary means of stopping all unlawful practices. Rather, private litigation by farmers and ranchers who are

actually harmed is the best way to guarantee effective and widespread enforcement of the run-of-the-mill violations.

### 1. USDA enforcement

USDA has tried to use enforcement proceedings before administrative law judges as a substitute for rulemaking. Using their I-know-it-when-I-see-it approach, and without the guidance of regulations, USDA has sued major meatpackers for preferential pricing (In re Beef Marketing Group) and unlawful market retaliation (In re Farmland National Beef Co.), for example. While those cases were mid-to-late-1990's exceptions to the historic "lack of any enforcement rule" at USDA, they failed to succeed primarily due to the lack of regulations defining unlawful practices under the Act. The administrative law judges hearing these cases had no regulations to guide their decision making and were left to ad hoc decision making. Because of those enforcement failures in the recent past, USDA is even more reluctant to litigate and has not begun to propound necessary regulations.

Even if USDA was willing to, and able to (funding and expertise-wise), increase enforcement activities, only the most significant cases would be undertaken – those with precedent setting potential. This is the history of enforcement in other antitrust contexts at DOJ and FTC. While this approach would be laudable if undertaken, there is no prospect that USDA can address all unlawful activities in the countryside.

### 2. DOJ enforcement

There is a process by which DOJ may be called upon by the Secretary to bring an enforcement action under the Act in federal district court.<sup>9</sup> However, to OCM's knowledge, this process has never been utilized. Again, the best case scenario is that this mechanism of enforcement would be limited to precedent setting cases, rather than run-of-the-mill violations.

### 3. Private litigation

The Act allows producers to engage in private litigation in pursuit of damages caused by packer harm.<sup>10</sup> Private litigation historically holds the most promise for comprehensive enforcement. This is because the incentive is extremely strong for those actually harmed by unlawful activities to pursue a remedy. However, the number of private cases has been very small since private suits were allowed in 1976.

The reason that farmers and ranchers have been unable to prosecute private suits is that there are no attorneys fees provisions or treble damages provisions under the Act. The Sherman and Clayton Acts have such provisions and, thus, private enforcement has complimented public enforcement. Without these provisions, the cases are too expensive to undertake due to their complex nature and the vigorous defense of packers. The solution is to amend the Act to allow farmers who win a suit to receive attorneys fees and treble damages. This is not a sop to trial attorneys, it is a provision needed for farmers to gain effective legal representation.

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<sup>9</sup> See, 7 U.S.C. §224.

<sup>10</sup> See, 7 U.S.C. §209.

### C. Solutions within USDA

Rulemaking and enforcement of the Act must be given a higher priority at USDA. This high priority must be accompanied by more professionalism, focus and funding directed at competition and fairness issues. Currently, GIPSA is a small, underfunded corner of the vast USDA bureaucracy. Field investigator recommendations for enforcement activity must go through several layers of bureaucratic scrutiny before final approval – and final approval for significant action usually does not occur.

Again, an analogy to the FTC is helpful. In the late 1960's, the Federal Trade Commission was justly criticized for being ineffective and unprofessional. A Nader Report and an American Bar Association report criticized the FTC for: poor leadership, lack of direction, aimless enforcement, and squandered resources. The fundamental question was whether the agency should be abolished or reformed.<sup>11</sup> The FTC chose to implement the solutions recommended in the ABA report.

In a June 12, 2001 speech before the American Antitrust Institute, current FTC chairman Timothy J. Muris recalled those thirty-years-ago changes:

*For consumer protection, the Report prescribed vigorous law enforcement and a national role in developing consumer protection policy. More specifically, it recommended that the agency:*

- *Focus enforcement on serious consumer problems, especially fraud.*
  - *Mount a more effective campaign against deceptive advertising.*
  - *Strengthen its remedies and reduce delays.*
  - *Provide industry guidance and incentives for compliance and self-regulation.*
- *Undertake studies, issue reports, and make legislative recommendations directed at pressing consumer issues.*
- *Work with state and local consumer protection agencies.*
- *Make consumer education part of the agency's mission.*

*For competition, the Report prescribed that the Commission use its unique history and institutional advantages - those not available to the Department of Justice Antitrust Division - to advance competition policy and enforcement. More specifically, the Report recommended that the agency:*

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<sup>11</sup> See, Muris, Timothy J., "Robert Pitofsky: Public Servant and Scholar," Speech to the American Antitrust Institute, June 12, 2001. (available at [www.ftc.gov/speeches/muris/muris010612.htm](http://www.ftc.gov/speeches/muris/muris010612.htm)).

- *Use the "full panoply" of its institutional tools to make competition policy - doing research, publishing studies, bringing cases, and making use of the intersection of competition policy and consumer protection authority.*
- *Formulate national competition policy by using the administrative process to adjudicate cases.*
- *Make policy involving "unsettled" areas of the law.<sup>12</sup>*

Thus, the FTC became far more effective and respected.

GIPSA is in a similar position to the old, ineffective FTC. It currently suffers from poor leadership, lack of direction, aimless enforcement, and squandered resources. However, it can use the tools at its disposal to provide focus and effectiveness, including: rulemaking, studies, legislative recommendations and enforcement. It can take advantage of the confluence of its producer protection authority and competition authority to set national policy towards a more fair, accessible, transparent and competitive market infrastructure.

Congress can facilitate this process by creating an undersecretary level position at USDA with the following (or similar) title: Office of Special Counsel for Competition and Producer Protection. The position should be filled by an attorney experienced in such matters, appointed by the president with the advice and consent of the Senate. That office, under this scenario, would house all USDA authority and personnel relating to agricultural competition and fairness such as the Packers & Stockyards Act, the Agricultural Fair Practices Act, and the Mandatory Price Reporting Act. The office would have the authority to propound regulations, initiate enforcement proceedings, interact with the Department of Justice, conduct studies and recommend legislation.

The goal should be an FTC-style remake of USDA-GIPSA. USDA is the largest agency after the Department of Defense. It engages in a wide variety of activities other than antitrust-style enforcement. If Congress agrees with farmers and ranchers that competition and fairness policy is a priority, then the USDA structure should reflect that priority and be empowered with the resources and leadership. The creation of an Office of Special Counsel for Competition and Producer Protection would greatly assist in accomplishing that goal.

### **III. Conclusion**

There is no credible argument to be made that the livestock markets are working properly. There is no credible argument to be made that the regulatory and enforcement regime is equal to the task before it. Congress should dispense with the past fascination with efficiency as a dominant goal.

Rather, Congress should focus on creating and maintaining a livestock market infrastructure in which all producers, of whatever size, can participate on equal terms without displacement by captive supplies. Congress should focus on market facilitating rules based upon fairness, access,

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<sup>12</sup> Id.

transparency and competition. The access and widespread participation on the internet, the U.S. highway system and the stock markets should be the governing metaphors or analogies.

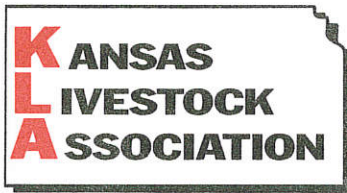
The proper analysis when balancing market facilitating rules with claims of losses in efficiency is as follows: First, the focus should be on creating a market system that is fair, accessible, transparent and competitive. The internal logic here is separate from efficiency. Second, if efficiency is raised as a negative factor, the following four questions must be asked before balancing the efficiency argument with the anticipated market facilitation effects: (1) Are the claimed efficiency gains/harm real? (2) Are the efficiency gains directly related to the market practice at issue? (3) Is there no other way to achieve the claimed efficiency gains? (4) Are the efficiency gains likely to be passed on to consumers or farmers, or is market power likely to obstruct passing the gains on to others. If the efficiency gains are real, related to the practice at issue, achievable in no other way, and likely to be passed on to consumers/producers, then we can quantify what efficiency gains are relevant and weigh them against the positive effect of the market facilitating rules contemplated.

Legislation should take away the ability for dominant firms to game the system. Captive supplies are the primary mechanism for such manipulation. Rather than requiring proof of past harm, the regulatory approach should look to the incentives in the system. Stated another way, Congress should focus on preventing future harm that is likely to occur because of the incentive and ability to manipulate price or engage in other strategic conduct that would be profitable to a firm but contrary to the public interest.

Thus, the packer ownership ban should be passed. The Enzi captive supply bill should be passed. Any efficiency claims attached to captive supplies are both unproven and eclipsed by the market disruption caused by the practice.

An Office of Special Counsel for Competition and Producer Protection should be created at the undersecretary level within USDA. That office should take over all competition, producer protection, and price reporting functions. That office should also be infused with leadership that can remedy the problems of poor leadership, lack of direction, aimless enforcement, and squandered resources. In doing so, that office can make use of the tools at its disposal including: rulemaking, studies, legislative recommendations and enforcement.

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## TESTIMONY

To: The House Agriculture Committee  
Representative Dan Johnson, Chairman

From: Mike Beam, Senior Vice President

Date: February 24, 2003

Subject: HB 2167 - Ownership of livestock

*The Kansas Livestock Association (KLA), formed in 1894, is a trade association representing over 6,000 members on legislative and regulatory issues. KLA members are involved in many aspects of livestock production, including cow-calf/stocker enterprises, cattle feeding, seedstock production and diversified farming operations.*

*Kansas ranked third nationally with 6.6 million cattle on ranches and in feed yards as of January 1, 2002. The state's beef industry consumes 72% of the corn, 16% of the soybeans, and 60% of the hay grown in Kansas. Cattle sales typically generate nearly two-thirds of all annual agricultural receipts.*

The Kansas Livestock Association (KLA) sincerely appreciates the opportunity to comment on this legislation. Changes in fed cattle marketing practices easily have generated more discussion, frustration and turmoil among KLA members than any other single issue during the past twenty years. The result of these debates consistently has yielded the same policy position within our association. KLA urges its members to consider the negative effects of certain marketing arrangements, yet guards its members' freedom of choice to utilize their own marketing program as they see fit. (See attached policy resolutions.)

In summary, HB 2167 would prohibit large-scale packers from directly or indirectly engaging in the ownership of livestock for the production of livestock or livestock products for more than 14 days prior to slaughter. Furthermore, it would be unlawful for a packer to enter into a contract to purchase cattle for slaughter using a formula or grid pricing mechanism if the packer failed to negotiate a base price prior to the livestock being committed or scheduled for slaughter. The bill would exempt entities that operate as marketing cooperatives outlined in KSA 17-1616. A person who suffered a financial loss as a result of a violation of the act could bring a civil action for treble damages. As written, the attorney general or county or district attorney could prosecute violators and seek injunctions.

KLA is opposed to HB 2167 because the bill (1) would restrict and/or prohibit marketing arrangements currently used by our members; (2) would impose state marketing guidelines that would be inconsistent with, and in contrast to, existing

ederal rules governed by USDA; and (3) likely would violate the Commerce Clause of the United States Constitution.

To fully understand our concerns, you first must realize a fundamental result of the packer restrictions found Section 2. If a state law limits a packer's business practices, it also restricts a producer's marketing options. The open-ended "indirectly be engaged" prohibitive actions would cast a great deal of uncertainty as to what types of fed cattle marketing arrangements could continue in this state.

For example, it is common for feeders to enter into a forward contract with a packer to deliver a specified group of animals at 120 days prior to delivery. Usually this price is determined by a specified deferred fed cattle contract price at the Chicago Mercantile Exchange. This arrangement was especially attractive last December, because producers could use this risk management tool to retain ownership and market their yearlings as fed cattle this spring at a profitable price level. Without this marketing tool, lenders would have been more inclined to require the cattle be sold off grass last fall at an unprofitable cash price. Could this marketing arrangement with a packer be illegal because of the 14-day restriction in Section 2? I contend it would be illegal if the state chose to enforce this proposed law.

The marketing practice in subsection (b) of Section 2 is more specific. You'll hear from one of our members this afternoon that has experience with formula and grid pricing arrangements that would be made illegal by the enactment of HB 2167.

Please note, the prohibitions of using formula or grid pricing without a base price negotiation would apply only to cattle. Why should this bill outlaw a marketing practice for cattle and not limit the activity for other meat species?

We encourage this committee, and the full legislature, to exercise caution when considering any legislation that seeks to restrict, limit, or regulate livestock marketing within the borders of Kansas. Last month, a United States District Court declared an Iowa law forbidding pork processors from directly or indirectly owning, operating, or controlling pork production as unconstitutional. We'll provide this committee with a copy of the decision and Iowa law. It is important to note that the judge ruled the Iowa law violated the Commerce Clause of the United States Constitution because it "discriminates against interstate commerce on its face, in its effect, and in its purpose for no reason other than economic protectionism".

The plaintiffs in this case claimed discrimination because the Iowa law authorized cooperatives to conduct certain business practices that were specifically forbidden by other business entities. In the end, this discrimination argument was not an issue because the judge determined the law was unconstitutional because of other facts. This argument does create an interesting question. Would this bill, and other proposed Kansas marketing bills that exempt cooperatives, be at risk if subsequently challenged in court?



Let me close with a few additional thoughts. Authorization for a \$4.5 million study of livestock marketing issues was included in the recently passed federal omnibus appropriations bill. One matter that will be reviewed is the impact of federal restrictions similar to this bill. Does the Kansas Legislature want to jump ahead of USDA with bills like HB 2167 without a more thorough analysis?

Enacting a state law such as HB 2167 would chart a new course for Kansas's government and the state's livestock industry. Rest assured, passage of this bill would be the start of ongoing legislative battles about what "indirect" ownership really means, is a one million animal unit threshold still appropriate, what is meant by formula or grid pricing, and how will the state deal with new entities that restructure to fit within the exemption offered by cooperatives.

While we respect the intentions of the proponents to HB 2167, we sincerely believe this legislation would cause far more problems than any perceived benefits. We respectfully ask the committee to not advance this legislation.

Thank you.

## **22. MARKETING (2003)**

WHEREAS, the livestock industry is facing a changing marketing situation and many recognize the negative effects of non-negotiated sales, captive supply and cash selling on averages as evidence that the current fed cattle marketing system has broken down, and

WHEREAS, many in the industry see the practice of selling all cattle for one money without regard to carcass merit as a major impediment in the value discovery process, and

WHEREAS, too many consumer beef eating experiences today are unsatisfactory, and the beef cattle industry must move toward the production of a more consistent, higher quality beef product in order to recapture market share.

THEREFORE, BE IT RESOLVED, the Kansas Livestock Association supports changes to the current marketing system that improve the value discovery process.

BE IT FURTHER RESOLVED, the Kansas Livestock Association suggests to its members they consider the negative effects of non-negotiated sales and the benefits of selling on a negotiated carcass merit basis, but regardless of how Kansas Livestock Association members choose to market their cattle, the Kansas Livestock Association shall continue to guard its members' freedom of choice to conduct their own business and utilize their own marketing program as they see fit.

## **23. KLA STATEMENT OF OPERATING PRINCIPLES (2003)**

WHEREAS, the Kansas Livestock Association believes the livestock industry is best served by the process of free enterprise and free trade, and

WHEREAS, even with its imperfections, free trade is relatively more equitable than regulated and subsidized markets which retard innovation and distort production and market signals, and

WHEREAS, regulated and subsidized markets disadvantage some producers in favor of others.

THEREFORE, BE IT RESOLVED, the Kansas Livestock Association is opposed to attempts to narrow the business options or limit the individual freedom of livestock producers to innovate in the management and marketing of their production unfettered by additional government regulations.



Since 1894

## TESTIMONY

To: House Ag Committee  
Representative Dan Johnson, Chairman

From: Larry Jones, KLA President

Date: February 24, 2003

Subject: **HB 2167**

*The Kansas Livestock Association (KLA), formed in 1894, is a trade association representing over 6,000 members on legislative and regulatory issues. KLA members are involved in many aspects of livestock production, including cow-calf/stocker enterprises, cattle feeding, seed stock production and diversified farming operations.*

Mr. Chairman and members of the committee, I am Larry Jones from Holcomb, Kansas, and I am the current President of the Kansas Livestock Association. My brother and I are the owners of JO Cattle Company. Our operation includes a cow-calf operation, farming, and feeding our cattle for slaughter at our family feedlot. Our family operation has been actively involved in KLA for nearly 100 years, and we have been members of Cattle-Fax, the pre-eminent market analysis service for our industry, for over thirty years. I say this to emphasize that we pay close attention to our business and the factors influencing our markets. In KLA, our guiding principle is to obtain the facts as best we can understand them from the most credible sources and to make those facts - politically popular or not - available to our members upon which to base our policy positions. After reviewing all the facts, our members took action to oppose bills like HB 2167.

We realize there are those in our industry who firmly believe a bill like HB 2167 would improve the market. We respect their freedom to hold that opinion, even though it has not prevailed in our policy deliberations. Our members have voted repeatedly to make marketing decisions without the interference of government regulation. The losses suffered by our members the past several years were the most severe ever.

It is easy to see now why now...basic supply and demand. Attached to my testimony is an analysis by Cattle-Fax detailing the \$17 per cwt. increase in cattle prices that has occurred in less than five months. Let me put that in perspective...the increase in fed cattle prices during the last five months would be equivalent to the DJIA moving from 8,000 to over 10,000. What you will see in the attachment is that our industry had record production in 2002. Compared to 2001, we produced 19 million more pounds PER WEEK! As much as I would like to blame someone else for our losses, including packers, the facts don't support such a conclusion.

That is not to say we can't improve our industry's marketing system. That's why last year I was among a group of cattlemen appointed from the four largest cattle feeding states with the goal of

improving our marketing system. Organizations represented on the Four-State Working Group were KLA; Texas Cattle Feeders Association; Colorado Livestock Association; Nebraska Cattlemen's Association and the Kansas Cattlemen's Association. We began with the idea that captive supply was the "problem". We heard from analysts and business people from other commodity industries, including those involved in cooperative marketing. Our work took all summer and into the fall. I'll make a long story short by saying that by the time we had the facts, it was the consensus of our group that getting the government involved in deciding who can own cattle was not the answer. Instead, it was the unanimous conclusion of our group to recommend to our respective producers to consider using the services of Consolidated Beef Producers, a cooperative group-selling service based in Amarillo, Texas, as an option to market fed cattle.

Prominent market analysts and objective, credible economists tell us that 'captive supply' [cattle owned or contracted by cattlemen to packers longer than seven days prior to slaughter] has not been a major factor influencing market movements...up or down. These marketing methods were not what moved the market downward from the \$80's to the \$60's in the mid 1990's and in 2001, and they are not responsible for the recent rise of prices to record levels where they are today. The dominant driver is overall supply...the volume of beef tonnage on the market.

South Dakota and Missouri have tried similar legislation with disastrous effects on producers. Also, a federal court recently ruled an Iowa law banning packer feeding was unconstitutional. Just a few months ago, our members lost millions of dollars when the government got involved in mandatory price reporting, and now we are faced with a cumbersome mandatory country-of-origin labeling law. With this in mind, we respectfully ask you to not give serious consideration to this, or any bill, which would restrict or narrow our marketing choices for our cattle. Thank you.

# WHY HAS THE MARKET IMPROVED \$17/CWT. SINCE SEPTEMBER?

The cash fed cattle market has had an impressive rally since the first full week of October 2002 when cash fed cattle price averaged \$64.03/cwt. to the first week of February 2003 when fed cattle prices averaged \$81.09/cwt. That's a \$17.06/cwt. rally in just 19 weeks. During that same period, the light Choice boxed beef cutout rallied from \$109.17 to \$135.02 – up \$25.85/cwt. For perspective, last year's spring highs for fed cattle prices and the light Choice boxed beef cutout were \$74.28/cwt. and \$124.64/cwt., respectively. If the spring highs are in for both fed cattle prices and light Choice boxed beef then they have exceeded last year's highs by \$7/cwt. and \$6/cwt., respectively. Remember that the fourth quarter of 2001 was filled with outside factors that impacted beef and fed cattle demand. The factors included the effects of the terrorist attacks of September 11<sup>th</sup>, the discovery of BSE in Japan during September and resulting 30% to 40% decline in exports to Japan and the slowing of the U.S. economy.

In determining why this rally in prices has occurred one only has to look as far as the two economic components of price: supply and demand. Simply put, supplies tightened and demand improved. Both of these factors combined to help improve prices at the fed cattle and wholesale levels. The following is an analysis of the supply and demand components of price and how each contributed to the rally.

To fully understand how and why supplies tightened during the fourth quarter of 2002 and first quarter of 2003 several factors must be analyzed. These include the marketable supply of fed cattle and profitability situation of the feeding industry during 2001 and the first three quarters of 2002, and the placements, shipments, and carryover supplies of cattle before and during the rally.

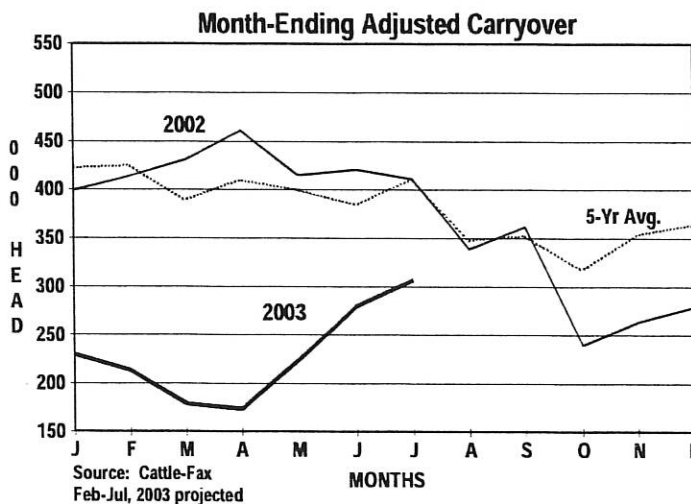
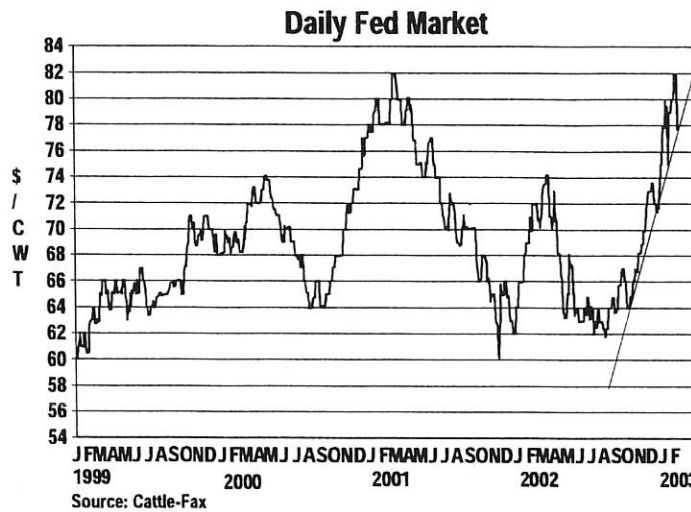
During the summer of 2001, placements of cattle into feedlots were abnormally large causing a record large supply of marketable fed cattle for September through December of that year. Shipments of fed cattle and cattle slaughter during this same period were not large enough to keep carryover

supplies from growing to record proportions. Following the events of September 11, 2001, beef as well as other meat products became harder to merchandise as consumer and business spending declined. At the same time carcass weights began to increase further compounding the supply problem that the industry faced – this was the beginning of uncurrentness and lack of profitability for the feeding industry. The situation continued to worsen as first quarter 2002 placements of cattle into feedlots were larger than a year earlier and heavy carcass weights continued to set records. The net result was that weekly average beef production set new monthly records in eight of twelve months during 2002, prices suffered due to over supply, and the feeding business lost more than \$2 billion in equity.

This loss of equity led to a reduction in weekly average feedlot placements by about 14% from April through July, as many operations chose not to place as many cattle. Carryover supplies peaked unseasonably during April, and then declined from May through October. Carryover supplies but weren't

back to manageable or more normal levels until July and August 2002, but record heavy carcass weights still plagued the supply situation and more than offset the decline in the number of head of cattle in the carryover. The smaller second quarter placements reduced the number of marketable fed cattle from September through December 2002 by about 16%, so all the industry had to do was keep shipping cattle at a reasonable pace and eventually carryover and total fed cattle supplies would decline, which they did.

Average carcass weights increased 20 lbs. per head to 758 lbs. during 2002, and cattle slaughter increased 361,000 head to 35.731 million head. Combined, these increases added 1 billion pounds to beef production during 2002 compared to 2001. The record beef production of 2002 totaled 27.1 billion pounds. The past four years have had the four largest beef production totals on record. Spread throughout the year, the increase in beef production equaled 19 million pounds per week,

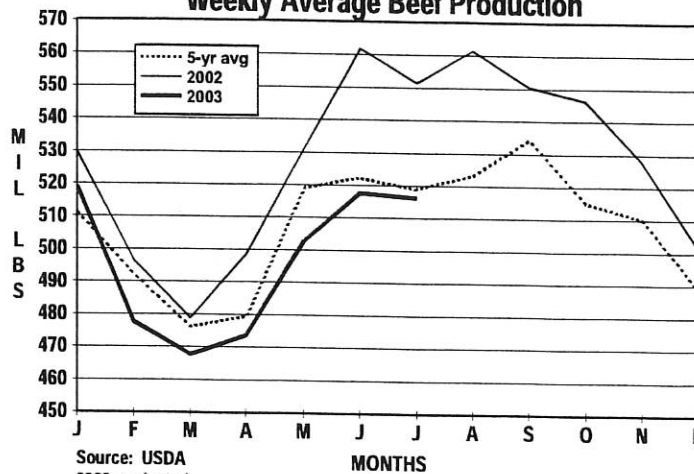


putting 2002 weekly average beef production at 528 million pounds per week. On average, each 10 million pound increase in weekly average beef production reduces fed cattle prices by \$2/cwt. and being uncurrent in marketings reduces prices by about \$1/cwt. on an annual basis. Additional impacts on fed cattle prices came from better beef demand that was worth about a \$1/cwt. on an annual basis, but was offset by \$1/cwt. lower hide and offal values. Combined, these factors

suggested that fed cattle prices during 2002 should have been about \$5/cwt. lower than a year earlier. During 2002, fed cattle prices averaged \$67.46/cwt. versus \$72.29/cwt during 2001. So, the lower fed cattle prices seen during 2002 were what would have been expected given the outcome of the supply and demand situation.

During the fall and early winter of 2002, fed cattle supplies began to decline substantially, but fed cattle slaughter and beef production remained above a year earlier. Fed cattle supplies as measured by the Cattle-Fax monthly beginning inventory were 17% smaller than during the same period in 2001 and carryover supplies were 42% smaller than a year earlier. The decline in monthly fed cattle supplies was brought about by fourth quarter shipments that were only 6% smaller than a year ago that had to be sourced from smaller placed against supplies (down 20%) and the smaller carryover totals (down 42%). As the fourth quarter 2002 developed, supplies got continually tighter and this scenario continues to play out today. The fed cattle marketing rate (shipments divided by available supply) had to accelerate just to keep cattle slaughter and beef production levels in line with demand. In doing so, available supplies of fed cattle and eventually boxed beef supplies were rapidly depleted. This shift in fed cattle supplies and corresponding decline in carryover supplies increased cattle feeder bargaining position seasonally even though weekly average beef production during the fourth quarter of 2002 ended up being about equal with a year earlier. The increase in bargaining position and demand during the fourth quarter of 2002 combined to be worth an additional \$5.50/cwt. to fed cattle prices compared to the fourth quarter of 2001. Increased cattle feeder bargaining position and better demand for fed cattle each contributed about half of the increase. Hide and offal values during this period were about \$0.75/cwt. higher. This analysis suggests that demand for fed cattle and better feeder bargaining position, in light of expected smaller supplies, was largely responsible for the first three months of the current rally. Better beef demand helped packers move wholesale beef prices 3.8% higher during the fourth quarter. This created a margin shift between packers

**Weekly Average Beef Production**



Source: USDA  
2003 projected

and retails similar to the shift between cattle feeders and packers.

So, what has changed since the first of the year to further fuel the rally in fed cattle prices? Available fed cattle supplies tightened to the point that slaughter rates and resulting beef production had to decline. The rapid marketing pace of the fourth quarter, record low carryover supplies, and third quarter placements that were about 7% smaller than the previous five-year average

resulted in January and February fed cattle supplies that were 25% below a year earlier. These smaller fed cattle supplies and slightly lighter carcass weights have resulted in weekly average cattle slaughter and beef production totals during January and February were 2% and 3% smaller, respectively. The decline in weekly average beef production for January and February, compared to a year ago, will be about 15 million pounds per week, which in these two months is worth about \$3.50/cwt. plus the increase of hide and offal values of more than \$1/cwt. This accounts for the increase due to smaller supplies but does not factor in demand and additional margin shift between cattle feeders and packers for January and February which combined totaled to be about \$4.25/cwt. better for fed cattle prices than during January and February 2001. The bottom line is that both supply and demand have played a significant role in the recent rally in fed cattle prices.

Weekly average beef production has declined 60 million pounds per week from September 2002 (which averaged 550 million pounds per week) to the end of January and early February 2003 (which averaged 480 million pounds per week). This seasonal decline in production was worth about \$12.00/cwt. to fed cattle prices. A more current cattle feeding industry and resulting better bargaining position, and stronger beef demand have each added about \$2.00/cwt. to fed cattle prices. Higher hide and offal values have added an additional \$1.00/cwt. to fed cattle prices. All combined the current market should be trading about \$17.00/cwt. higher (or near \$80) than fed cattle prices during September and early October 2002.

During the past two years the market has faced record beef supplies, record total meat supplies and several negative outside factors, but in spite of these things the market has been efficient in responding to supply and demand. The fed cattle market has been very efficient at evaluating changes in supply and demand and determining appropriate prices levels over time. Changes in supply and demand will continue to impact this market, as will outside factors, and the efficient interpretation of the factors will continue to changes prices and send economic signals back through the system.



*Your Partner for Quality Beef Production*

Testimony to the Kansas House Agricultural Committee  
Representative Dan Johnson, Chairman

In opposition to

**HB 2167**

by

**Tracy Brunner**  
Ramona, Kansas  
February 24, 2003

My name is Tracy Brunner and I appear today as an opponent to House Bill 2167. As a matter of introduction, my brothers, my parents and I operate a family farming, ranching, and feeding operation near Herington, Kansas. We farm, own a cowherd, provide breeding stock to commercial cow/calf producers, and feed cattle out for slaughter at our own local feed yard. This family business currently involves the fourth and fifth generations of Brunners involved in Kansas's agriculture production.

We too are constantly searching for ways to compete in a business that is changing more rapidly than ever before. There is now a swift collection and dissemination of information due to supermarket scanners, the internet, cellular phones and other modes of new technology. We will do our best to adapt in this environment. We can't afford, however, to have the state legislature narrow our marketing options as suggested in HB 2167. It appears this bill would make illegal our existing practices and limit our opportunities for the future.

For example, we often use a "grid pricing" system to market our fed cattle. On most occasions we use a method where we do not negotiate the base price as referenced in HB 2167. While it is not a perfect system, it is efficient and allows us to deliver an improved product to consumers.

I want the committee to know that our family has never fed cattle for a packer. There could be a time, however, that we find this a profitable and preferable option. Should my family be denied this opportunity because of a state law? I would hope the state legislature would not adopt such a policy.

I believe the future of beef production is to change our marketing practices in a way that adds value to quality animals. The value discovery process is in an evolutionary search for a more efficient way to determine a base price for finished cattle. Any law beyond what is currently in effect at the federal level will stymie innovation and make it even more difficult to find solutions to today's challenges.

I encourage this committee to reject HB 2167. Thank you for considering my views.

**House Agriculture Committee**  
**Hearing on HB 2167**  
**February 24, 2003**

My name is Patrick Hubbell, I represent Tyson Foods, Inc. I appear today in opposition of House Bill 2167. Tyson Foods acquired Iowa Beef Producers (IBP) in 2002, gaining a substantial interest in the state of Kansas. IBP employees 6,425 workers throughout the state and maintains operations in Garden City, Hutchinson, Emporia and Olathe. In 2002, IBP operations in Kansas purchased more than 1.8 million cattle at a cost of \$1.47 billion.

HB 2167 would violate the Interstate Commerce Clause (ICC), as similar legislation did in Iowa that banned packers from owning livestock in Iowa. In addition, the federal government is reviewing similar provisions, such a law would be more appropriate at a federal level in order to avoid violations of ICC, or to put producers in one state at a disadvantage over other states.

Prohibiting packer ownership could cause serious financial detriments to those independent producers who raise livestock for packers under contracts, and who have financed operations based on these contracts.

The forced liquidity of livestock and livestock operations by the packers could have three negative impacts:

- (1) markets could be flooded with livestock in liquidation phase lowering prices;
- (2) packers could have to go through fire sales to sell off livestock operations, lowering the appraised value of operations overall affecting producers net worth; and
- (3) fewer buyers for feeder calves would exist.

Almost all contracts that Tyson/IBP enter into with producers are requested by producers. Producers ask to enter into these contracts for a number of reasons, including time and savings. Custom feedyards can take substantial amounts of time to negotiate the base price on each load of cattle. By entering into formula agreements producers do not have to spend hours each week marketing cattle, and can instead spend the time on improving efficiencies and the quality of their product. HB 2167 would hurt producers who requested these relationships in the first place.

A majority of people, including producers, are hesitant to have the government interfere with their freedom to contract, which would take away one of the basic rights American businesses have today. Additionally, the provision to make violators of the bill subject to a misdemeanor with the possibility of treble damages is also a concern. If authority is extend not only to the attorney general, but also each county attorney litigation expenses for even the smallest matter, such as discovery on a producer complaint, would add cost to the industry that will be pushed back on the producers with lower prices, or on to customers with higher prices

Packer/producer agreements are efforts by producers to work with packers to create the most consistent safe products for consumers. HB 2167 would hamper the efforts of other producers



and packers to work together to create the safest and best products for consumers and compete against other similar products.

We would urge the committee to vote "no" on HB 2167.



## ***Kansas Farm Bureau***

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### ***PUBLIC POLICY STATEMENT***

#### **HOUSE COMMITTEE ON AGRICULTURE**

**Re: HB 2167 – Banning packer ownership and requiring negotiated base prices.**

**February 24, 2003  
Topeka, Kansas**

**Presented by:  
Leslie Kaufman, State Director  
KFB Governmental Relations**

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Mr. Chairman and members of the Committee, thank you for the opportunity to comment on HB 2167 which places a ban on packer ownership of cattle and swine and requires a negotiated base price in formula and grid pricing arrangements. I am Leslie Kaufman and I serve as the State Director of Governmental Relations for Kansas Farm Bureau (KFB). KFB is the state's largest general farm organizations and represents agricultural producers through the 105 county Farm Bureau Associations across Kansas.

Section 2(a)(1) of the bill imposes a ban on packer ownership of cattle and swine more than 14 days prior to slaughter for entities processing more than 1,000,000 animal units per year. In January of 2003, the voting delegates at our annual convention of the American Farm Bureau Federation removed policy language calling for the Packers and Stockyard Act to be amended to prohibit packer ownership of livestock for more than 14 days prior to slaughter except for cooperatives or entities owned by cooperatives and packers who slaughter less than 2% of total U.S. slaughter. Additionally, the delegates recommended the AFBF Board of Directors direct a study on the livestock industry and a committee has been appointed to examine:

- Banning packer ownership of livestock;
- Encouraging packers to participate in the marketplace to ensure an open and competitive cash market;
- The effectiveness of mandatory price reporting; and
- Examination of the current Packer and Stockyards Act and ways in which may improve its effectiveness.

House Agriculture Committee  
February 24, 2003  
Attachment 11

The study is to be presented to the AFBF Board of Director at their June 2003 meeting. Until the study is complete and the AFBF Board takes further action, Farm Bureau will oppose the movement of any legislation with respect to a ban on packer ownership of livestock. Thus, we cannot support section 2(a)(1).

Our AFBF delegates did approve language based on a recommendation forwarded by the Kansas Farm Bureau members that contracts and marketing agreements should specify a negotiated base price before commitment to delivery. They were clear in reaffirming our support for the rights of producers and packers to enter into formula pricing, grid pricing and other marketing arrangements and contract relationships. The policy noted above is directly related to the provisions in section 2(b)(1) and we do partially support the concept espoused in that section. There is at least one significant distinction between the language (b)(1) and our Farm Bureau policy – ours is permissive and the bill's is mandatory.

Although we do not agree with portions of HB 2167, we do appreciate that enforcement of the bill is vested in the court system and not administrative procedures. Our members have strong reservations about the growth in civil penalty authority and believe it should be the court system's role to enforce laws and regulation, rather than relying so heavily on agency action.

We do appreciate the opportunity to speak to you today on these issues important to Kansas' livestock producers. Thank you.

*Kansas Farm Bureau represents grassroots agriculture. Established in 1919, this non-profit advocacy organization supports farm families who earn their living in a changing industry.*