2010 Annual Report

Packers & Stockyards Program

United States Department of Agriculture
Grain Inspection, Packers and Stockyards Administration

MISSION:

"To protect fair trade practices, financial integrity, and competitive markets for livestock, meat, and poultry."

March 2011

2010 REPORT HIGHLIGHTS

- ***Packers and Stockyards Program (P&SP) performance and efficiency remain strong***. In 2010, P&SP's measure of industry compliance with the Packers and Stockyards Act of 1921 (P&S Act) was 80 percent and the program's efficiency, the average number of days to conduct an investigation, was decreased by 14 percent or 98 days (see pages 25 and 27).

- ***P&SP enforcement is more effective and efficient.*** P&SP closed 42 percent more investigations and regulatory actions in 2010 than in 2009, with a 10 percent reduction in the number of investigations and regulatory actions remaining open at the end of the fiscal year (see pages 27 and 28).

- **P&SP increased collection of civil penalties from entities that admitted their violation, based on cases prepared by P&SP and prior to any formal litigation.** A total of 38 cases were settled through the use of stipulations resulting in civil penalties of $127,787.00, an increase of 315 percent over $30,775 in penalties collected from stipulations in fiscal year 2009 (see page 12).

- ***U.S. Department of Justice (DOJ) and U.S. Department of Agriculture (USDA) joint competition workshops.*** Workshops were held across the country to discuss competition and regulatory issues in the agriculture industry. The workshops addressed the dynamics of competition in agriculture markets, including buyer (monopsony) power and vertical integration. They examined legal doctrines and jurisprudence, as well as current economic learning regarding competition and the application of the antitrust laws to the agricultural sectors (see page 33).

- P&SP provided statistical summary of data on investigations as specified by Congress in the 2008 Farm Bill, titled Food, Conservation, and Energy Act of 2008 (see page 30).

- P&SP standing advisory teams with financial and scales and weighing expertise were developed and used in part to develop new Standard Operating Procedures (SOP's), workflows, and software developer instructions (see page 32).

- P&SP established a confidential information policy team to create new policies to provide a guidance document and a short training class for all P&SP staff. The activity is complete and each employee has signed an acknowledgment form to confirm completing the training (see page 32).

- P&SP completed the 2010 Assessment of the Livestock and Poultry Industries as required in Section 415 of the P&S Act (see page 40).

Overview—P&SP operates under the authority of the P&S Act. P&SP is administered by a Deputy Administrator, who reports to the Administrator of the Grain Inspection, Packers and Stockyards Administration (GIPSA). The Deputy Administrator provides leadership to five program directors, two in the Washington, D.C., headquarters and three in regional offices located in Atlanta, Georgia; Aurora, Colorado; and Des Moines, Iowa.

Each regional office director manages a Business Practices Unit, a Financial Unit, and two Resident Agent Units, which enforce the P&S Act through regulatory actions and investigations. The director also oversees the administrative Program Support Unit, and the Western Regional Office director oversees the Central Reporting Unit, which processes industry entities' annual reports filed with P&SP.

Unit Level Activities—To ensure compliance with the P&S Act, P&SP agents conduct two broad types of activities: investigative and regulatory. Investigations are carried out when a violation of the Act appears to be occurring. Regulatory activities are monitoring activities to determine if a regulated entity is complying with the P&S Act and result in rectification of identified noncompliances. For example, in 2010, P&SP conducted 671 weighing verifications (including "checkweighs") that found 77 violations, in which cases P&SP initiated corrective measures; 297 custodial account audits resulted in account corrections worth slightly more than $2.3 million.

Strategic Business Plan—Management of P&SP is achieved through tactical short-term operational and long-term strategic goals. These goals are communicated to all employees primarily via a Strategic Business Plan. The 2010 plan identifies four strategic business goals that articulate longer term strategies into annual operational objectives. These goals are:

1. Increase the level of compliance with the P&SP Act through preventative regulatory actions.
2. Attain compliance through investigations and enforcement.
3. Implement directives, policies, and regulations and perform industry analyses that effectively and efficiently keep pace with the changing livestock, meat, and poultry industries.
4. Improve organizational efficiency and effectiveness.

Objectives under goals (1) and (2) are implemented at the field and headquarters levels and yield P&SP's overall aggregate performance measure, which is the industry's compliance rate with the P&S Act in any given year. Compliance in 2009 remained at 80 percent, as in 2008, versus 73 percent in 2007. In 2009, goal (3) was attained by the development of new competition monitoring programs, expanding existing rules for production and poultry contracts to cover swine contractors, and defining feed weighing standards for swine contractors.

The investigations conducted in accordance with goal (2) also provide information on the level of efficiency that P&SP achieves when obtaining compliance with the P&S Act under goal (4) of the Strategic Business Plan. Efficiency is defined as the average number of days from the beginning date of an investigation until it is closed within P&SP or until the investigation is referred to the USDA Office of the General Counsel (OGC) for possible formal prosecution. Investigation efficiency has improved since 2006—investigations remained in P&SP 98 days in 2010 compared to 114 days in 2009. P&SP closed 1,769 investigations in 2010. An additional 85 investigations were closed in 2009 that had been referred to OGC, including 4 that OGC had referred to the DOJ.

Initiatives—P&SP is carrying out several initiatives to achieve greater industry compliance with the P&S Act and to increase efficiency in achieving compliance. Some examples of major initiatives include formation of internal advisory teams to address selected issues, enhancements to the Employee Library and continued emphasis on employee training, and additional enhancement to P&SP's management information systems and the capabilities to generate performance data from those systems. P&SP also worked on several proposed new regulations during the year, and participated in a series of workshops with DOJ to discuss competition and regulatory issues.

Accomplishments—In fiscal year (FY) 2010, P&SP finalized four regulations related to swine contractor activities, scales and weighing, registration terms, and poultry contracts. Two proposed rules were also published related to required scale tests and the 2008 Farm Bill. P&SP also completed the implementation of a paperless case management software system in December 2009.

Industry Assessment—P&SP completed the annual assessment of the industries regulated under the P&S Act, which is based on data from the annual reports filed by regulated firms covering the firms' 2009 fiscal year. The assessment indicates that the four largest firms' share of the total value of livestock purchases (i.e., aggregate industry concentration) has been relatively stable over the past 5 years but declined in 2009. Four-firm concentration ratios by volume of steer and heifer slaughter increased slightly in 2009.

Concentration in poultry slaughter has trended upward since 2000. Cow and bull slaughter concentration increased from 1999 to 2007 then declined in 2008 and remained steady in 2009. Concentration in hog slaughter increased sharply in 2003 was stable until a decline in 2006, returned to the previous level in 2007 and 2008, then declined slightly in 2009. Concentration in sheep slaughter has varied since 1999 from a low of under 65 percent in 2004 to a high of over 70 percent in 2008, but declined slightly in 2009 to just over 69 percent, a little more than one percentage point higher than in 1999.

Trends in the marketing practices of packers vary by species. The volume of carcass-basis purchases of cattle trended upward from 1998 through 2002, fell to a lower plateau in 2004 through 2006, and then increased in 2007 and 2008 and remained about the same in 2009. By comparison, carcass-basis purchases of hogs have trended slightly upward since 2001.

The use of committed procurement methods by the largest beef packers has continued to trend upward since 2005, although the rate of increase appears to have slowed in the last few years. Marketing agreements represent the largest portion of committed cattle procurement.

Industry Concerns—Markets for cattle and hogs sold for slaughter are increasingly reliant on self-referencing to determine the market price. That is, many livestock are sold through contract transactions that reference a price determined in the negotiated segment of the slaughter livestock market. In addition to the various benefits from contract transactions, a major benefit is a reduction in the cost of price discovery. This occurs because traders are letting someone else do the negotiating but still referencing the price as a public good. These users are benefiting from what is termed the free rider effect in the economic literature on public goods. Due to a lack of exclusivity, public goods are provided at below optimal levels. The proportion of trade accounted for by the negotiated market in the Texas-Oklahoma regional fed cattle market, where a significant proportion of trade is between large feed lots and packers, declined 13 percentage points from mid-2008 to mid-2009. The Iowa-Minnesota market, which has a high proportion of large swine contractors, had roughly 2 percent of its volume traded in negotiated transactions in mid-2009 and instances are observed where a handful of transactions set the day's price. Whether these markets accurately determine a price that reflects supply-demand conditions or determine a price that reflects unintentional or intentional strategic behavior is the subject of many complaints received by GIPSA. For example, frequently hog prices are being determined by firms' definitions of its base hog, the hog that does not earn premiums or discounts, and based on this definition firms either raise or lower the price of hogs when they trade.

GIPSA has received an increase in complaints related to price determination in poultry tournament systems. A range of grower complaints has been received. For example, growers have complained about poultry integrators replacing the growers in a settlement group after settlement and then the integrator recalculates the wage rate paid to growers. Another type of complaint is related to integrators segregating a subset of a settlement group and then making a different management treatment available to the subset, which adversely affects the payment received by the remaining group. A feature of price determination in competitive supply-demand driven markets is the impartiality in establishing the value each party receives from the transaction based on supply-demand conditions outside the control of either trading partner. The determination of the grower's wage rate in any given poultry tournament has the potential to be highly partial, and equity considerations are observed to depend on the benevolence of the poultry integrator in any particular settlement.

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OVERVIEW OF THE PACKERS AND STOCKYARDS PROGRAM

This section provides a brief overview of the Packers and Stockyards Program's (P&SP) authority and responsibilities under the Packers and Stockyards Act of 1921 (P&S Act), P&SP's position within the organizational structure of the USDA, and P&SP's own internal organization.

Authorities and Responsibilities

Under the P&S Act, the Secretary of Agriculture (Secretary) has authority over businesses engaged in the marketing of livestock, wholesale meat, and poultry. The Secretary has delegated this authority to the Packers and Stockyards Program for regulation and enforcement. Regulated business entities include livestock market agencies (which include auction markets), livestock dealers, stockyards, packers, swine contractors, and live poultry dealers (this includes most poultry slaughterers or "poultry integrators"). These businesses assemble and process livestock and poultry, and move their products through the first manufacturing, or meatpacking, phases of the livestock and poultry marketing channel. Livestock producers, feedlots, and poultry growers at the originating or upstream ends of the market channels and most retailers at the opposite downstream end of the market channel are not under P&SP's jurisdiction.

The P&S Act prohibits unfair, unjustly discriminatory, and deceptive practices. It also prohibits regulated businesses from engaging in specific anti-competitive practices.

In addition to describing unlawful behavior, the P&S Act mandates certain business practices by regulated industries. For example, market agencies and dealers must be registered; market agencies, packers (except those whose average annual livestock purchases do not exceed $500,000), and dealers must be bonded to protect livestock sellers; and buyers must make prompt payment for livestock. To protect unpaid cash sellers of livestock, packers are also subject to trust provisions that require that livestock inventories and receivables or proceeds from meat, meat food products, or livestock products be held in trust for unpaid cash sellers until payment is made in full. A similar provision applies to live poultry dealers.

P&SP uses its statutory authority to investigate alleged violations of the P&S Act and regulations, and prosecutes violations identified through those investigations in administrative actions prosecuted by USDA's Office of the General Counsel or through referrals to the DOJ.

Under the Food Security Act of 1985, States may establish central filing systems to pre-notify buyers, commission merchants, and selling agents about security interests against farm products. P&SP administers the section of the statute commonly referred to as the "Clear Title" provision by certifying the filing systems of States that apply to P&SP for certification. P&SP does not have authority to de-certify States unless a State requests such decertification, and it does not have the authority to determine if States are maintaining certification standards.

Packers and Stockyards Program's Business Organization

The Packers and Stockyards Program is administered by a Deputy Administrator, who reports to the Administrator of the Grain Inspection, Packers and Stockyards Administration (GIPSA). In addition to the P&SP, the GIPSA Administrator oversees the Federal Grain Inspection Service (FGIS). Within the USDA, the GIPSA Administrator reports to the Under Secretary for Marketing and Regulatory Programs (Figure 1).

P&SP's appropriated budget for 2010 was $23.7 million, a $1.3 million increase over 2009 levels. P&SP used the increased funds to hire new field staff.

Table 1. P&SP Appropriated Budget for Fiscal Years 2006-2010

Year	2006	2007	2008	2009	2010
Funds ($K)	20,257	20,172	20,901	22,412	23,692

The Deputy Administrator of the P&SP provides strategic leadership to five program directors, two in headquarters in Washington D.C., and three in regional offices in Atlanta, Georgia (Eastern Regional Office); Aurora, Colorado (Western Regional Office); and Des Moines, Iowa (Midwestern Regional Office) (Figure 2). As of October 2010, P&SP had 166 full-time staff.

Each regional director manages an administrative Program Support Unit and four program units: a Business Practices Unit, a Financial Unit, and two Resident Agent Units. The units are organized based on responsibilities under the P&S Act and are designed to capitalize on the tactical advantages of placing staff in the field. Each unit is comprised of 5 to 10 staff members. Each unit has a supervisor who reports to the Regional Director. Staff members supervised in the regional offices are responsible for conducting investigations and regulatory activities such as business audits, weighing verifications, and day-to-day industry monitoring. These activities are described in greater detail in the next section.

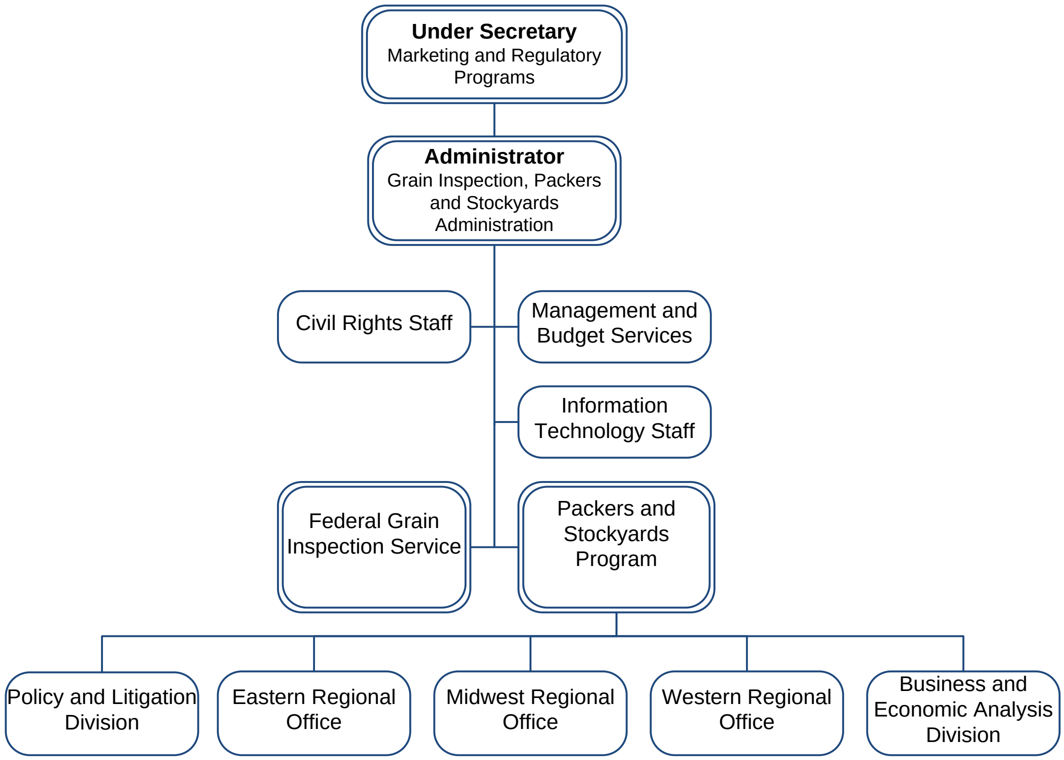

Figure 1. GIPSA Administration Organizational Structure

Each regional office is expert in one or more species of livestock or in poultry. The Eastern Regional Office focuses on poultry, the Midwestern Office on hogs, and the Western Regional Office on cattle and sheep. Forty resident agents, who report to the regional offices, are located throughout the country to provide core services nationwide (Figure 2). The geographically dispersed resident agents enable P&SP to maintain close contact with the entities that it regulates, which are similarly dispersed throughout the United States (see Figures 3 through 6).

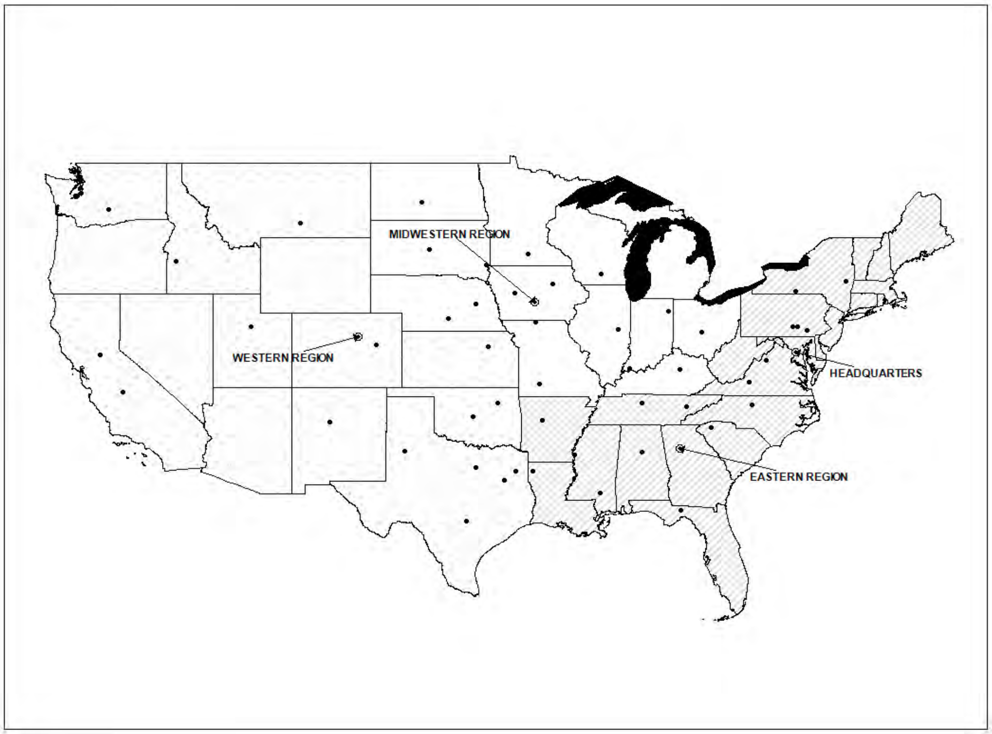

Figure 2. P&SP Regional Office and Resident Agent Locations

Figure 3. Location of Livestock Packers (Headquarters only for multi-plant firms) Subject to the P&S Act

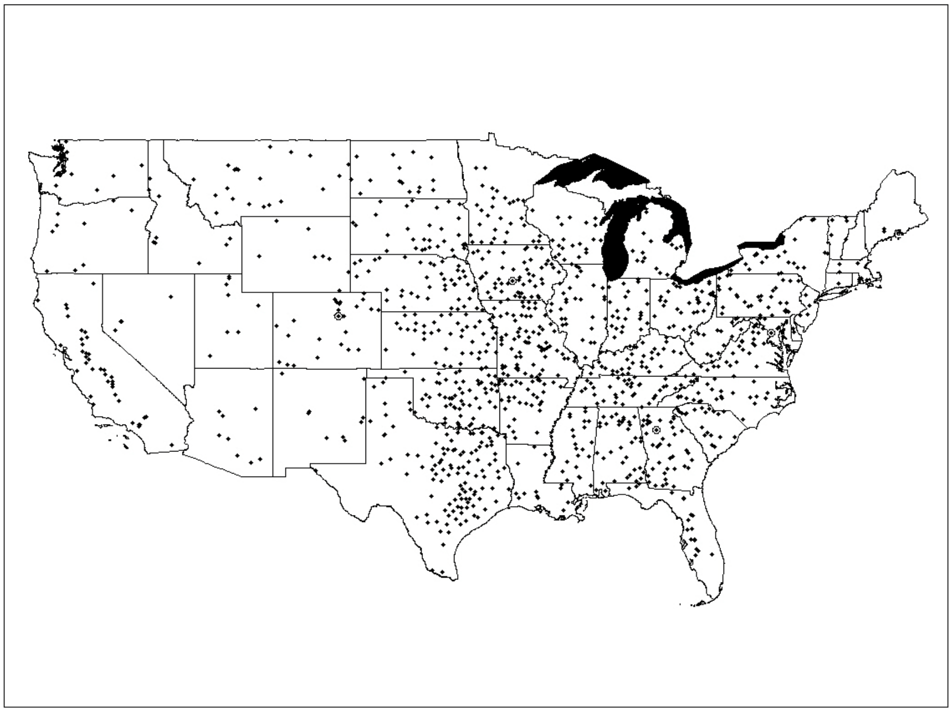

Figure 4. Location of Livestock Markets and Firms Selling on Commission Subject to the P&S Act

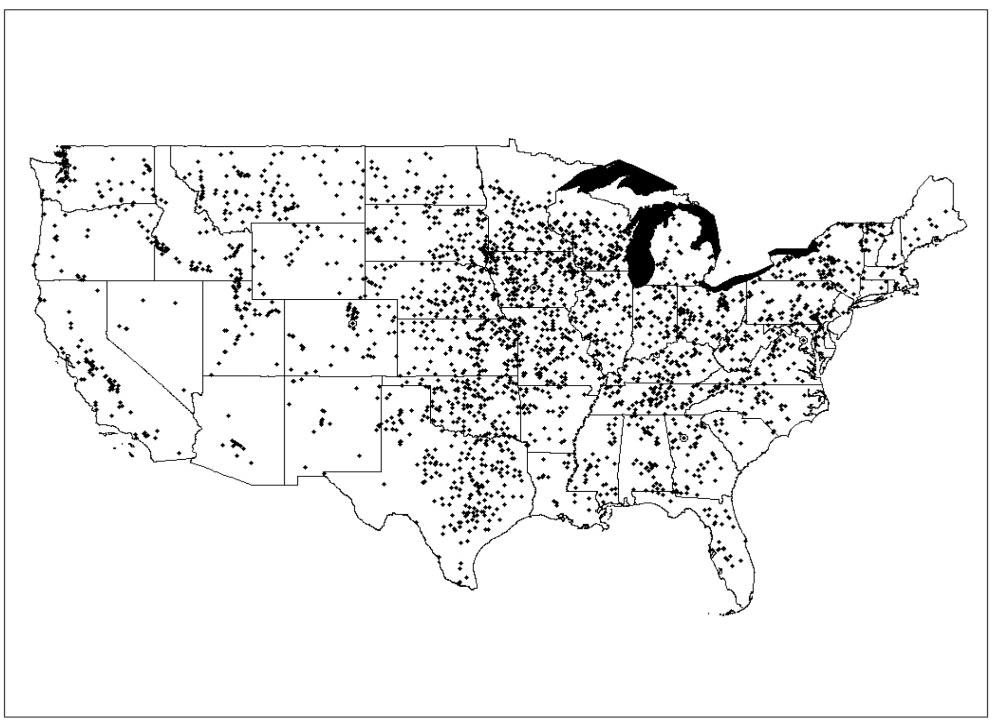

Figure 5. Location of Livestock Dealers Subject to the P&S Act

Figure 6. Location of Live Poultry Dealers (Headquarters only for multi-plant firms) Subject to the P&S Act

P&SP conducts two broad types of activities at the unit level to enforce the P&S Act: investigative and regulatory. Investigations are conducted when there is reason to believe a violation of the P&S Act is occurring or has occurred. Regulatory activities are monitoring activities carried out to determine if a regulated entity is complying with the Act. The most in-depth, complex investigative and regulatory activities are performed by the regional offices' Business Practices or Financial units. The Business Practices units include legal specialists, economists, and marketing specialists who focus on competition and trade practice issues. The Financial units are staffed with auditors who investigate and undertake regulatory activities related to enforcing the financial requirements of the Act. Routine activities are conducted by resident agents who work closely with regulated businesses and livestock sellers and poultry growers.

Investigations at a firm level may be a follow-up to previously identified violations of the P&S Act. In other instances, investigations may be initiated in response to complaints from industry participants, possible violations found while conducting regulatory activities on a business's premises, or possible violations found through other monitoring. Investigations may be conducted as rapid response actions to prevent irreparable harm to the regulated industries.

Members of the livestock and poultry industries and the public may report complaints and share concerns via a toll-free number (1-800-998-3447) or e-mail address (PSPComplaints@usda.gov). Individuals or firms with complaints about the livestock and poultry industries also are encouraged to call the appropriate regional office to discuss their concerns, anonymously if desired.

P&SP responds to all of these external contacts. P&SP also initiates investigations independently, for example, as a result of information obtained from monitoring industry behavior.

Regulatory activities include, but are not limited to, check-weighing; custodial account and prompt payment audits; procurement and marketing business practice reviews; registering market agencies, dealers, and packer buyers who operate subject to the P&S Act; assisting producers in filing bond and trust claims; analyzing trust and bond claims; and conducting orientations for new markets and new packers.

Regulatory activities also include market-level monitoring, which is generally conducted using data that are available in the public domain. Examples include, but are not limited to, monitoring fed cattle and hog prices and analyzing structural changes in the livestock, meat, and poultry industries. Monitoring activities have led to firm-level investigations. Regulatory activity may occur entirely or partially at an entity's place of business or at a Regional Office.

P&SP regulatory and investigative activities are categorized as generally addressing areas of competition, trade practice, or financial concerns. Program expenditures on investigations and regulatory activities are greatest within the financial area of enforcement (Table 2).

Table 2. Total Regulatory and Investigation Expenditures, 2001-2010

	Regulatory (K$)			Investigation (K$)		
Fiscal Year	Competition	Trade Practice	Financial	Competition	Trade Practice	Financial
2001		N/A		3,431	4,117	5,318
2002		N/A		3,575	4,290	5,541
2003		N/A		3,755	4,506	5,820
2004		N/A		3,905	4,686	6,053
2005		N/A		4,050	4,860	6,277
2006	----	6,705	----	1,775	2,640	3,869
2007	----	7,142	----	1,488	4,259	3,419
2008	----	3,664	----	330	6,220	6,238
2009	205	2,047	3,281	245	3,330	9,244
2010	81	1,342	4,463	388	4,928	8,621

Table notes: "N/A" indicates data not available. Prior to fiscal year 2006, regulatory activities and investigations were not differentiated; from 2006-2008, competition, trade practice, and financial regulatory activities were not differentiated.

P&SP's regulatory and investigative actions frequently find that entities are in compliance with the P&S Act. When violations are discovered, P&SP levies agency-established fines (stipulations) for admitted violations or pursues litigation through USDA's Office of the General Counsel (OGC) before a USDA Administrative Law Judge or through the DOJ. Litigation may result in a fine against the offending entity, or in suspension of the entity's P&S registration. Not all cases result in monetary penalties. In 2010, P&SP levied $127,787 in stipulations and an additional $341,027 in penalties through administrative law judges for a total of $468,814 (Table 3). Penalties obtained through DOJ actions, including penalties assessed by default, totaled an additional $346,705.

Table 3. Penalties Levied for P&S Act Violations, 2006-2010

Type Judgment	2006	2007	2008	2009	2010
Stipulations ($)	NA	9,750	23,275	30,775	127,787
Administrative Penalties ($)	196,350	404,150	657,770	364,700	341,027
DOJ Civil Penalties ($)	NA	36,500	51,240	59,580	346,705
Complaints Issued	25	50	46	40	50
Suspensions	0	0	0	19	6

Table note: Prior to 2007, administrative and DOJ penalties were combined. P&SP began using stipulations in 2007, in which entities agree to fines set by P&SP. P&SP settled 38 cases through stipulation in 2010.

Enforcing Business Practice Provisions

The regional Business Practices Units have responsibility for inspections and investigations of trade practice and competition provisions of the P&S Act.

Supported by resident agents, the units conduct investigations of alleged anti-competitive practices and unfair and deceptive trade practices by market agencies, livestock dealers and order buyers, slaughtering packers, live poultry dealers, and meat dealers and brokers. Economists and legal specialists in the units conduct competition investigations and regulatory activities. For example, an economist might monitor market and firm prices for indications of anti-competitive firm behavior. Marketing specialists conduct trade practice investigations and regulatory actions related to inaccurate weighing practices or carcass evaluation instruments and compliance with contracts. The competition and trade practice work conducted by these units is discussed in more detail below.

Competition

Investigations are a central activity of our competition program. P&SP investigates complaints alleging anti-competitive behavior such as attempted restriction of competition, failure to compete, buyers acting in concert to purchase livestock, apportionment of territory, price discrimination, price manipulation, and predatory pricing. P&SP's economists and legal specialists collaborate with USDA's OGC on all competition investigations. When the results of an investigation indicate that the evidence and circumstances support legal action, P&SP formally refers the case file to OGC for action.

P&SP conducts many activities that monitor changes in industry behavior in order to understand the nature of and reasons for changes, and to anticipate potential competitive issues that may result from those changes.

Details of specific, ongoing individual monitoring efforts are described in the next three sections.

Fed Cattle and Hog Market Price Monitoring

P&SP undertook a price monitoring initiative in response to market issues that evolved from the announcement of the first case of bovine spongiform encephalitis (BSE) in the United States on December 23, 2003. A national task force comprised of P&SP economists modified an econometric model in use since the mid-1990s that detected price differences in regional fed cattle markets. The statistical model relied on USDA’s Agricultural Marketing Service (AMS) publicly reported price data to assess regional price differences. If a statistically significant price difference was detected, P&SP initiated a regulatory review work plan to determine whether those price differences were caused by an undue or unreasonable preference or disadvantage in violation of section 202 (b) of the Act or by uncontrollable external factors, such as weather or other external macroeconomic conditions.

The current fed cattle market price program was first implemented in 2004, but has since evolved into an enhanced program that includes a weekly internal reporting regime and a detailed work plan to conduct in-depth investigations into possible violations of the Act if the initial regulatory reviews of price differences do not clarify whether they were caused by external market factors. The model and the historical database upon which the monitoring program is based have also been enhanced through further economic and statistical research activity conducted by P&SP economists.

The model is run weekly, and any price outlier that is not caused by certain technical statistical factors triggers a regulatory review by P&SP. If the regulatory review does not determine that the price outlier was caused by certain external factors or readily observable market conditions, then a formal investigation is initiated to determine the cause of the price outlier. The formal investigation involves deeper examination of the price data and cattle characteristics, and interviews with buyers, sellers, and other market participants.

The fed cattle price monitoring program initiated 16 regulatory activities in 2010, none of which indicated cause for investigation (Table 4).

Table 4. Regulatory Activities and Investigations Resulting From Weekly Statistical Monitoring of Fed Cattle Markets, 2006 - 2010

Fiscal Year	Regulatory Activities Initiated	Investigations Initiated
2006	25	6
2007	13	0
2008	19	4
2009	25	3
2010	16	0

P&SP continues to actively monitor market prices on a weekly basis and initiate timely regulatory reviews and investigations, if necessary, of observed market price anomalies.

Effective September 9, 2009, a statistical model similar to the fed-cattle model was implemented for daily monitoring of hog market prices for the three AMS barrow and gilt price reporting areas. These AMS market areas include Iowa-Minnesota, the eastern corn belt, and the modified western corn belt. AMS includes Iowa and Minnesota in its market reports for the western Corn Belt region, but to ensure non-overlapping markets, P&SP modified the territory to remove the Iowa and Minnesota hog transactions and prices from this region. Live and carcass prices are monitored, except in the modified western Corn Belt market, which only reports carcass prices. The model reported 23 daily price outliers for these five market prices during fiscal year 2010. All outliers were satisfactorily explained without initiating an investigation. Whether P&SP is monitoring fed cattle or hog prices, when the statistical model reports an outlier, an economist from either the Midwestern or Western regional office reviews the suspect price and makes a recommendation report, which is reviewed by an economist in each regional office, the originating Business Practices Unit’s supervisor, and an economist in headquarters. Based on the report and reviewer comments, the supervisor either closes the review or opens an investigation and requests individual firm transactions data from AMS.

Committed Procurement Review and Audit

P&SP monitors the use of “committed procurement” arrangements, which commit cattle and hogs to a packer more than 14 days prior to delivery. Each year, P&SP economists obtain fed-cattle and hog procurement data for the previous calendar year from the four largest beef packers and four largest hog packers. If the packers change their procurement arrangements with suppliers from previous years, P&SP also collects any new or modified written marketing agreements or contracts. P&SP economists review the contracts and, if necessary, discuss them with the packers to determine how the terms of the agreements relate to committed procurement categories of interest. Economists then classify, review, and tabulate the individual transactions data and calculate the reliance of the top packers on committed procurement methods. Finally, P&SP economists reconcile the calculations based on the detailed transaction data on committed procurement as reported by the packers in their Packer Annual Reports.

If there are significant differences between the transaction data and the Packer Annual Report submissions on committed procurement, the economists contact the packers to identify the cause of the discrepancy. If necessary, P&SP meets with the packers in person to discuss the packers' procurement methods and explain how they should be reported on the Packer Annual Report. These meetings foster a mutual understanding of the reporting of requirements for committed procurement and more reliable reporting and calculation of the packers' reliance on committed procurement methods.

Relying on written contracts and other information collected during the committed procurement reviews, P&SP agents analyze the various procurement and pricing methods used by hog and fed-cattle packers. Agents obtain and review contracts and agreements as necessary to determine if there have been any competition violations of the Act. The contracts are also used in procurement reviews of the packers to help determine if proper payment practices are being followed.

Poultry Contract Compliance Review Process

In FY 2010 P&SP conducted 77 poultry contract compliance reviews, over 50 of these reviews were based on a random sample. These reviews are based on standard operating procedures established in 2009 and are now included as a component of P&SP's performance measure (see Performance and Efficiency Measurement section). Poultry contract reviews may be initiated based on industry intelligence or complaints in addition to those conducted based on random samples.

The standard operating procedure for conducting poultry contract reviews is documented and includes links to the Packers and Stockyards Automated workflow software (PAS). P&SP agents follow these procedures when conducting poultry contract reviews. In general, the agent will collect relevant background information on the firm that is under review prior to conducting a site visit. Once on-site, the agent will conduct an interview and obtain copies of the grower contract being used at the plant location and 3 months of weekly ranking sheets for the contract. These documents are reviewed for consistency and adherence to P&S Act regulations. One week of payment data from the settlement sheet is selected as a random sample for a detailed review for accuracy and completeness. The results are compared to the firm's ranking sheets, settlement sheets, and payments to the growers to ensure consistency with the contract. If discrepancies are found, an investigation is opened. If the firm's practices are determined to be free of violation, the agent provides an exit interview indicating this to the firm's management.

Trade Practices

Firms that furnish stockyard services in commerce are required to post a notice that informs the public that the stockyard meets the definition of a stockyard under the P&S Act. Once posted, the stockyard remains posted until it is de-posted through public notice. P&SP meets with new auction market owners and managers as soon as possible as the market begins operations to ensure that market operators understand their fiduciary responsibilities under the P&S Act, and that they are operating in compliance with the P&S Act and regulations. These visits in the early stages of a market's operation also provide important protection to livestock producers who rely on the market to provide a nondiscriminatory and competitive marketplace. Similarly, P&SP conducts orientations for hog and poultry growout contractors who operate feed mills to ensure they understand the regulatory requirements for feed weights used to calculate producer/grower payments, thereby helping ensure that the feed weights and payments to producers are accurate.

P&SP reviews procurement practices to determine if unfair or deceptive trade activities are occurring in the procurement of livestock, meat, and poultry. The reviews assess pricing methods; payment practices; weighing of livestock, carcasses, and poultry; carcass grades used for payment; and accounting issued to sellers.

The P&S Act and regulations require markets, dealers, and packers to test scales at least semi-annually and file scale-test reports as evidence of scale maintenance. State and private companies test scales, and P&SP conducts weighing verifications and other investigations to ensure scale operators and firms subject to the P&S Act are properly using their scales and properly recording weights in the purchase and sale of livestock and poultry (Table 5).

Table 5. Weighing Inspections and Violations, 2007-2010

Type of Checkweigh	2007	2008	2009	2010
Inspections				
Market	137	188	245	215
Dealer	21	14	41	61
Packer	14	13	18	107
Carcass	106	82	148	140
Poultry	87	58	74	74
Feed	76	43	63	74
Total Inspections	441	398	589	671
Violations				
Markets	8	14	15	23
Dealers	0	1	3	6
Packers	0	0	1	15
Carcass	10	4	25	17
Poultry	4	4	11	7
Feed	5	5	14	9
Total Violations	27	28	69	77

Table Note: Market, dealer, and packer inspections are made for scales weighing live animals. Carcass and poultry inspections are made on scales that weigh carcasses in slaughter plants, and feed inspections are made on scales at feed mills.

A transaction made on false or inaccurate weights, including instances in which a dealer modifies the actual weight of the livestock or fails to pass on a shrink allowance, is an unfair and deceptive practice. Anyone who believes that an action of a stockyard, market agency, or dealer caused personal loss or damage in violation of the P&S Act may file a complaint seeking reparation (damages) with P&SP within 90 days of learning of the action that caused damages. The Act does not provide for reparation complaints to be filed against packers, live poultry dealers, or swine contractors.

Enforcing Financial Provisions

P&SP's financial units enforce the financial provisions of the P&S Act and regulations. These enforcement actions support the financial integrity and stability of the livestock, poultry, and meatpacking industries. Enforcement is carried out through reviews of annual and special reports, and onsite financial compliance reviews and investigations. Financial compliance reviews and investigations address solvency issues, payment to livestock sellers and poultry growers, bond claims, trust claims, and maintenance of custodial accounts. When P&SP identifies a potentially serious financial situation that may cause imminent and irreparable harm to livestock producers, rapid response teams are deployed immediately to conduct an investigation.

Under the P&S Act, most regulated entities must be solvent (current assets must exceed current liabilities). P&SP monitors the solvency of regulated entities by reviewing financial data in annual and special reports, and by onsite financial compliance reviews and investigations. P&SP notifies entities of their insolvencies and the immediate need to correct them. P&SP requires special reports from firms whose annual reports disclose insolvencies. In addition, P&SP conducts onsite financial investigations to ensure correction of reported insolvencies or other financial issues. Formal disciplinary action is initiated against firms when appropriate.

Market agencies selling livestock on commission (auction markets) must establish and maintain a bank account designated as a "custodial account for shipper's proceeds" to hold proceeds from the sale of consigned livestock. The commission firm or auction market acts as a fiduciary depositor to the account, and the funds in the account are trust funds held for the benefit of livestock sellers or consignors ("shippers"). P&SP monitors custodial accounts by reviewing annual reports from market agencies, analyzing special custodial account reports, and conducting onsite custodial account audits. When the monitoring reveals shortages in the account, P&SP acts to have the account balance corrected (Table 6).

Table 6. Number of Market Audits and Shortages Corrected Through On-Site Investigations, 2001-2010

Fiscal Year	Custodial Account Audits	Markets With Shortages	Corrected by On-Site Investigation
2001	322	156	6,313,383
2002	206	97	2,814,439
2003	262	92	2,055,203
2004	272	94	2,144,986
2005	252	102	5,269,525
2006	347	140	7,256,052
2007	296	99	2,037,080
2008	176	62	5,022,966
2009	383	181	2,581,725
2010	297	79	2,351,890

The P&S Act also establishes a statutory trust on certain assets of packers and live poultry dealers for the benefit of unpaid cash sellers of livestock and unpaid cash sellers or contract growers of live poultry grown for slaughter. Packer trust assets include all livestock purchased in cash sales, inventories, receivables, and proceeds from meat, meat food products, and livestock products derived from the purchase of livestock in cash sales. Poultry trust assets include all poultry obtained by live poultry dealers in cash poultry purchases or by poultry growing arrangements, inventories, receivables, or proceeds from such poultry or poultry products. Valid trust claims come before secured creditor claims in bankruptcy.

To be eligible for payment under the trust, a seller must file a claim with the packer or live poultry dealer and the Secretary within 30 days of the unpaid transaction. When a trust claim is filed, P&SP and OGC analyze the claim to assess whether it is timely and supported by adequate documentation. P&SP then makes the analysis available to the packer or live poultry dealer (the statutory trustee) and to trust claimants so that they can take any necessary action.

Additionally, all market agencies, dealers, and slaughtering packers purchasing over $500,000 of livestock annually are required to file and maintain bonds or bond equivalents for the protection of livestock sellers. To be eligible to receive payment under the bond, a seller (cash or credit) who does not receive payment for a transaction must file a bond claim within 60 days of the transaction. P&SP analyzes the claim to ensure it was filed within the timeline and supported by adequate documentation. P&SP provides its analysis to the principal and to the bond surety or trustee on a bond equivalent. In some instances the analysis is made available to all claimants to facilitate joint legal action. In some cases, claims may be made against and paid by both bond and trust assets.

Bonding requirements usually do not cover the entire loss sustained when a firm fails financially. Further, livestock sellers do not always determine the current bond status of smaller packers, dealers, and market agencies before selling livestock to them, making those sellers vulnerable to insufficient bond protection if the smaller firms fail. A large packer’s failure may impact auction markets and dealers from whom it purchased livestock and failed to pay.

Since 2001, an average of 13 dealers failed each year, with a range of 1 to 31 failures per year. During that same time period, producers received an average 16 percent payment of amounts owed to them, with recovery ranging from 0 to 56 percent (Table 7).

Table 7. Total Dealer Financial Failures and Restitution, 2001-2010

Fiscal Year	No. of Failures Open	No. of Failures Closed	Closed, Owed For Livestock ($)	Closed, Restitution From Bonds ($)	Closed, Restitution From Other Sources ($)	Closed Recovery (%)
2001	NA	11	2,841,305	317,444	24,786	12
2002	NA	11	3,271,962	618,764	60000	21
2003	NA	5	1,805,600	112,281	28,923	8
2004	NA	3	770,860	95,000	0	12
2005	NA	1	2,993,990	0	0	0
2006	NA	13	3,018,131	134,936	26,856	5
2007	NA	31	6,941,930	257,634	549,303	12
2008	NA	20	2,054,647	843,682	301,916	56
2009	NA	25	3,134,145	348,018	411,133	24
2010	2	7	213,332	20,000	0	9

Table Note: Starting in 2010 entries show the number of firms that have claims open at year-end and those cases that have closed at year-end; for past years, only total number of failures is shown. Dollar amounts for all years are for failures with claims closed as of most recent year-end, so historical data may have been updated to reflect any settlements after the year the failure occurred.

Auction markets may be especially vulnerable to a domino effect from dealer failures since many dealers purchase livestock from auction markets. The failure of a large dealer may impact every auction market that it failed to pay. Since 2001, an average of 6 auction markets failed per year. Consignors received average restitution of 47 percent payment of amounts owed to them, with a range of 22 to 98 percent (Table 8).

Table 8. Total Auction Market Financial Failures and Restitution, 2001- 2010

Fiscal Year	No. of Failures Open	Closed	Closed, Owed Consignors ($)	Closed, Restitution From Bonds ($)	Closed, Restitution From Other Sources ($)	Closed Recovery (%)
2001	NA	4	1,104,985	133,745	519,265	59
2002	NA	6	1,082,034	378,610	0	35
2003	NA	6	1,187,979	211,464	138,848	29
2004	NA	2	145,772	60,000	16,649	53
2005	NA	3	336,006	85,000	201,840	85
2006	NA	9	979,543	267,174	19,380	29
2007	NA	11	511,704	37,252	155,890	38
2008	NA	6	602,100	237,734	352,111	98
2009	NA	7	981,189	261,498	1,365	27
2010	1	4	20,901	4,547	0	22

Table Note: Starting in 2010 entries show the number of firms that have claims open at year-end and those cases that have closed at year-end; for past years, only total number of failures is shown. Dollar amounts for all years are for failures with claims closed as of most recent year-end, so historical data may have been updated to reflect any settlements after the year the failure occurred.

To maximize recovery, bond claims filed against packers are normally paid after claims made against the packer trust are dispensed. On average, in any one year, 4 packers will suffer financial failures owing livestock sellers an average of $5,669,636 (Table 9). The bond payout for packers was, on average, $788,810 or 14 percent of the valid bond claims. Additional restitution from packer trust assets and other sources bring the average recovery to 64 percent of total amounts owed, with a standard deviation range of 40 to 88 percent.

Table 9. Total Packer Financial Failures, Bond Payout, and Payout From Other Sources, 2001-2010

Fiscal	No. of Failures		Closed, Owed for Livestock	Closed, Restitution		Closed Recovery
				From Bonds	From Other Sources	
Year	Open	Closed	($)	($)	($)	(%)
2001	NA	1	81,735	50,000	0	61
2002	NA	3	17,007,170	6,394,489	5,838,750	72
2003	NA	3	2,508,633	225,952	1,238,772	58
2004	NA	1	2,056,869	142,752	369,507	25
2005	NA	2	5,032,018	55,000	1,977,761	40
2006	NA	5	755,550	35,267	683,834	95
2007	NA	6	4,118,456	40,000	4,083,946	100
2008	NA	4	3,498,895	0	1,588,620	45
2009	NA	12	15,676,349	196,208	9,999,228	65
2010	5	6	5,960,684	748,435	3,825,518	77

Table Note: Starting in 2010 entries show the number of firms that have claims open at year-end and those cases that have closed at year-end; for past years, only total number of failures is shown. Dollar amounts for all years are for failures with claims closed as of most recent year-end, so historical data may have been updated to reflect any settlements after the year the failure occurred.

As the livestock and meat industries evolve, P&SP continues to examine alternate ways to effectively regulate and monitor the industries and to effectively allocate its resources for planning and conducting regulatory compliance reviews. Most recently, P&SP adopted a statistical model to identify characteristics that place a livestock dealer, market, or packer at risk of financial failure. The characteristics identified are used, along with other firm information and market intelligence, to assess the need for financial audits.

PACKERS AND STOCKYARDS PROGRAM MANAGEMENT

The P&SP executes its management function through strategic, broad, multi-year goals and shorter term tactical annual objectives and activities. The primary method for monitoring and communicating these goals, objectives, and activities to all employees is a yearly Strategic Business Plan. The 2010 Plan identifies four broad strategic business goals:

- Increase the level of compliance through preventative regulatory actions;
- Attain compliance through investigations and enforcement;
- Implement directives, policies, and regulations, and perform industry analyses that effectively and efficiently keep pace with the changing livestock, meat, and poultry industries; and
- Improve organizational efficiency and effectiveness.

These broad strategic goals have remained constant while the tactical objectives and activities change to meet the longer term Program goals. The next section addresses how P&SP improves its performance and efficiency, and the results P&SP is demonstrating in achieving these goals.

The subsequent section presents management initiatives that span multi-year horizons and support achieving higher performance and efficiency. The initiatives include further enhancements and refinements to the ongoing business process re-engineering (BPR), and the development and use of a single, comprehensive P&SP database integrated with the workflow processes that were constructed as part of the Program's BPR.

P&SP has two smaller, though extremely important, management initiatives. The first is a training initiative. During 2010, new personnel with investigative and regulatory responsibilities participated in a formal week-long training presented by the Association of Certified Fraud Examiners. The course provides a baseline level of institutional and technical information for all P&SP agents. The training supplements the second initiative, a set of standard operating procedures that P&SP maintains online as a Web-accessible Employee Manual. The Employee Manual is one component of a set of instructions and guidance maintained online as a comprehensive employee guide to operations (see *Employee Library).*

Performance and Efficiency Measurement

P&SP measures its overall performance by annually measuring the regulated entities' compliance with the P&S Act. The performance measure encompasses activities P&SP conducts that directly or indirectly influence industry compliance. P&SP calculates the percent of industry entities in compliance using random samples designed to provide an estimate of compliance with a 90-percent confidence level. In 2010, P&SP maintained industry compliance at 80 percent. P&SP measures its efficiency at achieving industry compliance by the number of days it takes to complete the investigative phase (the time from complaint until a decision is made whether to refer the case to OGC or DOJ for possible enforcement action) of investigations. The time declined from 114 days in 2009 to 98 days for investigations closed in 2010. The time to conduct the investigative phase is only one measurement in the complex process of conducting an investigation. Additional information about efficiency measures follows the performance section.

Performance

P&SP's overall performance rate is a composite index of five program wide audit and inspection activities. In 2010 the index included: 1) poultry contract compliance reviews, 2) financial audits of custodial accounts of a random sample of firms, with the sample size designed to yield a 90-percent confidence level for the sample's compliance as an estimate for the entire population of regulated entities; 3) financial audits of the records used to verify prompt payments of a random sample of firms, also with sample size designed to yield 90-percent confidence for the estimated population compliance; 4) inspection of all scales and weighing practices in all packing plants purchasing more than 1,000 head per year; and 5) inspection of all carcass evaluation devices and carcass evaluation practices for a random sample of packing plants purchasing more than 1,000 head per year.

The aggregated industry compliance rate index reflects the statutory and regulatory compliance of the regulated industry with the P&S Act (Figure 7). The compliance rate has remained constant for the last 3 reporting years at 80 percent.

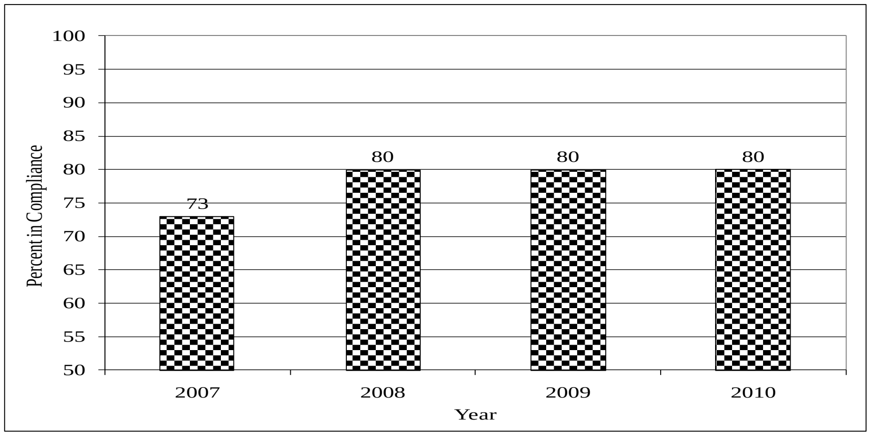

Figure 7. Aggregated Industry Compliance From Random Samples, 2007- 2010

Financial audits are carried out in accordance with general accounting standards and supervised by staff with certified public accounting status. Business practice inspections of scales and weighing practices are conducted based on standards established by the National Institute of Standards and Technology and supervised by staff trained in inspection procedures.

P&SP validates audits and inspections through internal compliance reviews, which were designed in conjunction with a private consultant, and adhere to the P&SP Standard Operating Procedures Manual published on the internal GIPSA Web page, "Employee Library."

In general the index measures three business practices and two financial practices for industry compliance with the P&S Act. While additional focus on activities to achieve industry compliance has resulted in increased compliance, general economic conditions within the industry will also affect year-to-year compliance. Weak economic conditions may increase the incentive for industry non-compliance in the financial components to a larger degree than in the business practice enforcement areas. The full effect of these external conditions on the compliance rate are not known, and to the degree that this measure only has a 4-year history, understanding the interaction of these variables on the overall compliance rate will be a challenge GIPSA confronts in future years. Additionally, GIPSA is just beginning to be able to use the data to make internal adjustments to ensure resources are effectively deployed to meet changing industry conditions due to external factors such as liquidity concerns.

The results of the individual component inspections and audits that comprise the aggregate index show a year-to-year increase in compliance rates in 2010 for three of the five areas reviewed. The poultry contract compliance review shows improvement from the initial rate of 60 percent in 2009 to 67 percent in 2010. Of the other four components, weighing practices compliance was nearly 96 percent and carcass evaluation compliance nearly 88 percent. Prompt pay and custodial compliance were 75 and 72 percent respectively (Figure 8).

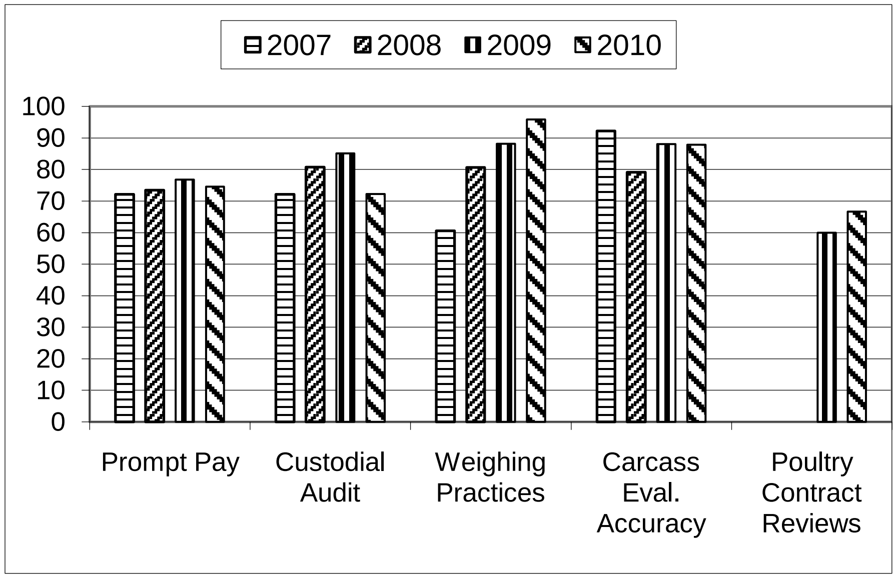

Figure 8. Performance Measure Components, FY 2007 through FY 2010

Efficiency

P&SP measures its efficiency as the time from initiating an investigation to closing it in P&SP, or until the investigation is referred to OGC. After referral, P&SP and OGC typically work together to develop adequacy and quality of evidence, determine witness availability, and complete final case preparation. The average days to conduct an investigation declined in 2010, after increasing in 2009 as a result of economic conditions triggering a higher proportion of complex financial failure investigations in 2009 (Figure 9).

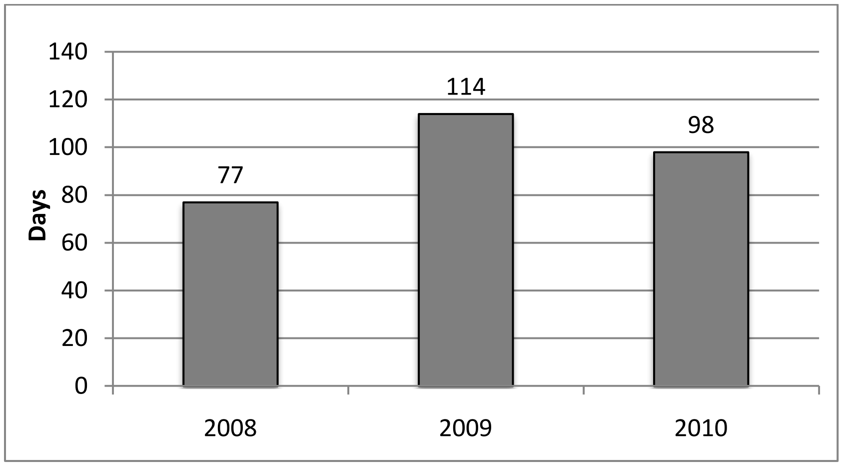

Figure 9. Days in Investigation From Opening to Closing or Referral to OGC, Investigations Closed in FY 2008 through FY 2010

The data in Tables 10 and 11 are total days to closure, averaged across cases closed by P&SP without referral to OGC and those cases closed after referral to OGC. Data in Tables 10 and 11 include the time in OGC while the data in Figure 9 do not. These data show that P&SP closed 42 percent more investigations and regulatory actions in 2010 than in 2009, with a 10 percent reduction in the number of investigations and regulatory actions remaining open at the end of the fiscal year. Total number of both types of actions that P&SP worked on during the year increased about 27 percent, from 4,353 in 2009 to 5,525 in 2010.

Table 10. Field Investigations and Regulatory Activities Closed and Activities Open at End of the Fiscal Year, Fiscal Years 2009 and 2010

	Number Activities		Percent	Average Days Open		Percent
Type	2009	2010	Change	2009	2010	Change
Investigations Closed	381	527	38.3	202	213	5.5
Investigations Open	243	233	-4.1	394	453	14.9
Regulatory Activity Closed	1214	1046	-13.8	35	27	-24.0
Regulatory Activity Open	58	27	-53.4	161	103	-36.0

Note: Field activities are conducted at the location of the regulated business entity.

Table 11. Office Investigations and Regulatory Activities Closed and Activities Open at End of the Fiscal Year, Fiscal Years 2009 and 2010

	Number Activities		Percent	Average Days Open		Percent
Type	2009	2010	Change	2009	2010	Change
Investigations Closed	678	1,327	95.7	126	88	-30.5
Investigations Open	548	735	34.1	156	142	-8.7
Regulatory Activity Closed	808	1,480	83.2	34	36	5.6
Regulatory Activity Open	423	150	-64.5	44	39	-12.5

Note: Office activities are conducted in GIPSA offices and are typically filing violations, e.g., failure to submit required documentation.

Investigations address a broad range of potential violations under the P&S Act and are grouped into three categories of competition, trade practice, or financial violations.

Competition violations often involve preferential treatment or restriction of competition, such as through apportionment of territory. Examples of trade practice violations include offenses such as unfair or deceptive practices, failure to register properly, tariff misrepresentation, and misuse of scales and improper weighing practices, including at any location where scales are used to weigh feed when feed is a factor affecting payment to livestock producers or poultry growers. Examples of financial violations include misuse of custodial accounts, failure to pay, and failure to pay when due (Table 12).

Table 12. Number of Closed Investigations in 2010 by Investigative Category

Investigative Category	Number
Competition	
Restriction of Competition	26
Preferential Treatment	5
Concentration/Industry Structure	2
Financial	
Bond Activities	602
Failure to Pay/Pay When Due	183
Solvency	157
Custodial Accounts	141
Annual Report	117
Packer/Poultry Trust	1
Trade Practice	
Registration/Jurisdiction	406
Unfair/Deceptive Practices	74
Weighing Practices and Scales	70
Grower Termination	23
Contract Poultry Arrangements	22
Procurement or Sales Review	11
Reparations	5
Inadequate or False Records	4
Merchandising	3
Tariff	2
Total	1,854

P&SP's regulatory and investigative actions often find that entities are in compliance with the P&S Act. When non-compliance is identified, P&SP either assesses fines or stipulations for admitted violations or pursues enforcement litigation with OGC. After referral but before filing, OGC works with P&SP to prepare the referred cases for filing and litigation before a USDA Administrative Law Judge or for referral to DOJ.

In fiscal year 2010, P&SP opened 2,110 cases, of which 2,068 were alleged violations for financial or trade practice behaviors. During the fiscal year, P&SP closed 1,769 cases without referring them to OGC (Table 13). An additional 85 cases were closed after referral to OGC, including 4 that OGC referred to DOJ.

Table 13. Number of Investigations Opened and Closed by Category and Enforcement Action, with Average Days to Complete Stages for Closed Cases, Fiscal Year 2010

	Average Days				
Status & Type	In PSP	Referral to Filing	Filing to Resolution	Start to Resolution	Number
A. Total Investigations Opened					
Livestock					
Competition					40
Financial					1,166
Trade Practice					767
Poultry					
Competition					2
Financial					5
Trade Practice					130
Total Opened					**2,110**
B. Total Investigations Resolved and Closed by P&SP					
Livestock					
Competition	218			218	31
Financial	86			86	1,130
Trade Practices	103			103	533
Poultry					
Competition	29			29	1
Financial	89			89	4
Trade Practices	130			130	70
Weighted Averages & Sub Total	**60**			**60**	**1,769**
C. Total Referred to OGC and Closed					
Livestock					
Competition w/ Enforcement Action	188	165	1,094	1,447	1
Financial w/o Admin Action	121			695	44
Financial w/ Enforcement Action	181	244	389	723	23
Trade Practice w/o Admin Action	414			546	6
Trade Practice w/Enforcement Action	80	270	204	599	4
Poultry					
Financial w/o Admin Action	127			919	1
Trade Practice w/o Admin Action	175			657	1
Trade Practice w/Enforcement Action	365	56	302	723	1
Weighted Averages & Sub Total	**162**	**239**	**385**	**699**	**81**
D. Total Referred to DOJ Through OGC and Closed					
Livestock					
Financial w/o Civil Action	**136**			**746**	**4**
Overall Weighted Averages and Total	**98**	**239**	**385**	**123**	**1,854**

Table Notes: Investigations opened during the fiscal year were not all closed by year end, and number of days per stage is only shown for cases that were closed during the fiscal year. Some of the closed cases were open in prior years. “w/o Admin Action” indicates that P&SP closed the case without filing a formal administrative enforcement action after referral to OGC. The “Referral to Filing” column in section C is the time that the case is in OGC prior to filing, whereas in section D this is the time that the case is in DOJ prior to filing after being sent to DOJ by OGC. Once the complaint is filed, indicated by the “Filing to Resolution” column, a case may go through a period before service is affected, may be resolved without hearing, or may go to hearing, subsequent decision by an Administrative Law Judge, appeal to the Department’s Judicial Officer, and/or appeal to the Court of Appeals.

Investigations resolved by P&SP are closed either through a finding of no violation, a Notice of Violation letter issued to the entity, or a stipulation settlement in which the respondent admits the violation and voluntarily agrees to a penalty. P&SP closed these cases within an average of 60 days, a reduction of more than 40 percent compared to 2009. Another 85 cases were resolved that had been referred to OGC. Cases are referred to OGC when P&SP determines that the investigation requires cooperation with OGC. Frequently in competition and cases involving large financial failures, OGC and P&SP continue to develop evidence with the goal of filing a complaint. The average number of days for cases referred to OGC is calculated based on whether the cases were referred to DOJ for prosecution. Cases not referred to DOJ required an average of 162 days in P&SP; cases referred to DOJ required an average of 136 days in P&SP. Table 13 represents only cases that were closed in 2010, and includes some cases that were initiated in years prior to 2010. As a result of referrals from P&SP, 29 administrative actions that had been filed by OGC were closed in 2010, and OGC closed an additional 52 cases after determining that evidence did not support formal administrative action. DOJ closed, without formal civil action, 4 cases that OGC had referred to DOJ.

Management Initiatives

In 2010, P&SP continued work on management initiatives that span multi-year horizons and support achieving higher performance and efficiency. Central to the management initiatives has been the core recognition that the people in P&SP are its primary resource and strength in achieving its mission. Organizational Assessment (climate) Surveys of the P&SP staff conducted in 2006 and again in 2008 by the U.S. Office of Personnel Management reflect the effect of this leadership philosophy. P&SP's average score across the 17 dimensions of the survey in 2008 improved significantly compared to 2006. The P&SP average score was 22 percent higher than the Government-wide benchmark average, and P&SP scored higher than the benchmark median in 15 of the 17 individual elements of survey. The participation of staff in major management initiatives has been a significant factor in improving employees' attitudes and morale.

Internal Advisory Teams

At the beginning of 2010, the P&SP management team had concerns about three major issues that became the focus of three separate initiatives. These issues included establishing an agency wide confidentiality policy, designing and implementing a new workflow to handle scale tests, and creating a new module to conduct financial reviews. The management team formed three subject matter expert teams to address these issues by the end of the fiscal year.

Confidentiality Policy Team

The confidentiality policy team's purpose was to create a detailed policy on employees' responsibility regarding confidential information collected during P&SP activities. A team of two attorneys, a legal specialist, and a resident agent met through several teleconferences and one face to face meeting to accomplish the task. The final policy specified various regulations that identified penalties for failing to adhere to the law of confidentiality, instructions to P&SP employees conducting agency activities, and definition of terms. The policy was implemented by the management team before the fiscal year end and with each employee signing an acknowledgement of the policy form.

Scale Test Team

Almost 2 years ago, P&SP implemented the Packers and Stockyards Automated System (PAS), an automated management information system to manage workflows and capture data including data for case file management. PAS was implemented in two phases with phase 1 including higher priority standard procedures and phase 2 incorporating remaining standard procedures such as scale tests. The P&SP management team solicited several subject matter experts from each region to focus on updating the standard operating procedure for scale test and work with PAS developers to design a workflow to automate the process. The team is currently finalizing the design for the workflow and will continue to assist developers until completion.

Financial Review Team

In order to standardize work across P&SP regions and units, several spreadsheets, called sub-process modules, were designed to ensure consistency. These modules are used to assist P&SP employees when conducting P&SP activities such as Investigations and Regulatory activities. However, there was a need to add a new module when conducting Financial Reviews. The P&SP management team created a cross regional team to design a sub-process module to handle financial reviews. The team recently submitted a module to the P&SP management team for approval and will implement a testing program for the next 6 months.

Employee Library

P&SP's online Employee Library is a complete resource for P&SP policy and employee guidance. The Library, which is the official documentation of all P&SP policy, contains general information about P&SP, standard operating procedures, work instructions, sub-process modules, training modules, and P&SP administrative instructions.

As another initiative for 2010, several upgrades and new features were added to the Employee Library. New features included navigation links to access a 211 page history of P&SP, information used by the Weighing and Grading Technical Team and Financial Technical Team, historical PAS training sessions and additional Standard Operating Procedures, and sub-process modules. Also added was an interactive staff directory that includes an organization chart linked to personnel photos for P&SP staff.

U.S. Department of Justice and U.S. Department of Agriculture *Competition Workshops*

A major initiative for 2010 consisted of five joint workshops that were held with the public as a result of cooperation between the DOJ and USDA. These were the first joint USDA and DOJ workshops to be held to discuss competition and regulatory issues in the agriculture industry. The goals of the workshops were to promote dialogue among interested parties and foster learning with respect to the appropriate legal and economic analyses of these issues as well as to listen to and learn from parties with real-world experience in the agricultural sector.

The workshops addressed the dynamics of competition in agriculture markets, including buyer (monopsony) power and vertical integration. The workshops examined legal doctrines and jurisprudence, as well as current economic learning. Additionally, they provided an opportunity for farmers, ranchers, consumer groups, processors, agribusiness, and other interested parties to provide examples of potentially anticompetitive conduct and to discuss any concerns about the application of the antitrust laws to the agricultural sectors. The workshops were transcribed and made available for public review, along with information submitted and written comments received. (Workshop documents are available at http://www.justice.gov/atr/public/workshops/ag2010/index.html.)

The first meeting was held March 12, 2010, in Ankeny, Iowa and focused on the issues facing crop farmers. However, there was considerable discussion regarding hog marketing. Other discussion topics included seed technology, vertical integration, market transparency, and buyer power. The second meeting was held May 21, 2010, in Normal, Alabama, and focused on production contracts in the poultry industry, concentration, and buyer power. The third meeting was June 25, 2010, in Madison, Wisconsin, and examined concentration, marketplace transparency, and market dynamics in the dairy industry. The fourth meeting was held August 27, 2010, in Fort Collins, Colorado, and focused primarily on cattle with concentration in livestock markets, buyer power, and enforcement of the P&S Act. A final meeting was held after the end of fiscal year 2010 on December 8, 2010, in Washington, D.C., and considered the discrepancies between the prices received by farmers and the prices paid by consumers. The workshops have enabled USDA to have a dialogue on issues relating to agricultural competition, which allows us to better understand the most important issues to producers and other stakeholders.

Regulation Status Update

P&SP worked on several proposed new regulations during the past year. Some of these were mandated by the 2008 Farm Bill, while the others arose from P&SP's own initiatives in response to perceived needs. The regulations are briefly summarized below according to their present stage of development.

Final Rules Published

Four final rules were published during fiscal year 2010. The first final rule, entitled "Scales; Accurate Weights, Repairs, Adjustments or Replacement After Inspection," was published on October 20, 2009. This rule amended regulation 201.71 (a), (b), and (d) to (1) incorporate by reference the 2009 (rather than the 1996) edition of **National Institute of Standards and Technology** (NIST) Handbook 44; and (2) add requirements that swine contractors must operate, maintain, and test scales according to the requirements of Handbook 44; use scales equipped with a printing device, which shall record weight values on a scale ticket or other document; and use only scales that are found, upon testing and inspection, to be in a condition to give accurate weights. The final rule was effective on November 19, 2009.

The second final rule, entitled “Poultry Contracts; Initiation, Performance, and Termination,” was published on December 3, 2009. This rule amended regulation 201.100 to (1) require livestock poultry dealers to promptly deliver to growers a copy of any poultry growing arrangement the growers entered into with the dealers; (2) include information about any Performance Improvement Plans or provisions for written termination notices in poultry growing arrangements; and, (3) notwithstanding a confidentiality provision, allow growers to discuss the terms of their poultry growing arrangements with Federal or State agencies, the growers’ financial advisor or lender, the growers’ legal advisor, accounting services representatives hired by the growers, other growers for the same live poultry dealer, and members of the growers’ immediate family or business associates. The final rule was effective on January 4, 2010.

The third final rule, entitled “Registration, Five-Year Terms,” was published on February 9, 2010. This rule amended regulation 201.10 regarding the registration of market agencies and dealers. Under the previous regulations, there was no expiration date or renewal process for the registration of a market agency or dealer under the Act. This rule establishes automatic renewal procedures with the filing of the annual report. Failure to file an annual report within a specified time period cancels an entity’s registration. The final rule was effective on March 11, 2010.

The fourth final rule, entitled “Swine Contract Library,” was published on April 2, 2010. The statutory authority for the library lapsed in September 2005 and was reauthorized in October 2006, by the Livestock Mandatory Reporting Reauthorization Act (Reauthorization Act). The final rule was effective May 3, 2010.

Proposed Rules Published

P&SP also published two proposed rules for public comment during fiscal year 2010. The first proposed rule suggested amending the regulations regarding the requirement that stockyard owners, market agencies, dealers, packers, or live poultry dealers that weigh livestock, live poultry, or feed have their scales tested at least twice each calendar year at intervals of approximately 6 months. This proposal would amend the current regulations to state that the 6-month interval in which scale owners must have their scales tested each calendar year is no longer approximate.

Specifically, the proposal would require that scale owners complete the first of the two scale tests between January 1 and June 30 of the calendar year. The remaining scale test would be required to be completed between July 1 and December 31 of the calendar year. In addition, a minimum period of 120 days would be required between these two tests. More frequent testing would still be required in cases where a scale does not maintain accuracy between tests. Finally, ‘‘swine contractors’’ would be added to the list of regulated entities to which the section applies. The comment period closed on October 23, 2009. The final rule has been prepared for publication.

The second set of proposed rules were mandated by the 2008 Farm Bill sections 11005 and 11006. For section 11005, the rules would establish requirements for contract termination, capital investments, and dispute resolution. A provision is also included that would require that a livestock or poultry contract must provide an option for arbitration when a dispute arises, if both parties agree in writing.

To comply with 2008 Farm Bill section 11006, the rules would establish factors to determine unreasonable preference, what is adequate notice to poultry growers of suspension of delivery of birds, when requiring an additional capital investment constitutes a violation, and whether a live poultry dealer or swine contractor has provided a reasonable period of time for growers to remedy a breach of contract. The proposed rule was published on June 22, 2010. A notice of extension of the comment period was published on July 28, 2010. The deadline for filing comments was November 22, 2010.

Real-time P&SP Performance Data

As P&SP developed the electronic case file management capabilities of the PAS automated management information system, real-time access to the data by P&SP employees was a large consideration. The software developers have previewed a “dashboard” concept which allows data to be easily accessed by users, sorted based on user preferences, and displayed in tables or graphs. The dashboard allows users to assess their workloads from an individual level, up to more general views at regional and agency levels.

Since PAS collects a vast amount of data, a series of dashboards will be released as specific needs are determined and designs are completed over time. As a test, P&SP released two dashboards that involve data for cases submitted to headquarters. The goal is to implement dashboards for P&SP major activities, Investigations and Regulatory Activities. The execution of these "dashboards" will be the final phase for fully implementing and completing development for PAS.

Employee Training

New Employees: GIPSA obtained training services from the Association of Certified Fraud Examiners (ACFE) after receiving notification from the Federal Law Enforcement Training Center (FLETC) that classes scheduled for fiscal year 2009 were canceled due to DOJ training priorities and resource availability. The ACFE offered training which closely aligns with the curriculum available at FLETC. The ACFE allowed P&SP the flexibility to build an agenda utilizing a core interviewing skills class and supplement it with important topics related to planning and conducting investigations and testifying in enforcement actions.

P&SP provided opportunities to attend three classes in February, June, and August 2010. Eighty-five P&SP agents attended the training in 2010 following one session in 2009, where 30 agents attended training. ACFE provided training for approximately 120 P&SP agents since its inception into P&SP in 2009.

The ACFE program was designed to give the P&SP agent the necessary tools to perform proper interviews while conducting an investigation. The course taught the attendees how to be more effective in asking questions and evaluating responses to obtain the best interview possible from the interviewee. The course also discussed a variety of methods for formulating questions to assist the attendees in dealing with any type of witness they will encounter. The attendees also learned the various verbal and nonverbal clues to deception, including changes in speech patterns, selective memories, oaths and character testimony, anatomical physical responses, and other indicators of deception.

The course covered all aspects of admission-seeking interviews. The attendees learned to prepare the interview location for effective communication, the best methods for confronting the suspect, and the initial steps of securing the admission. The attendees also learned how to ask admission-seeking questions and follow-ups based on the responses to the questioning. The session also included how to interrupt denials, depersonalize the victim, display physical evidence, and obtain admissions from respondents.

Leadership Development Program: GIPSA's Leadership Development Program (LDP) is a program conducted in conjunction with the Office of Personnel Managements. Its goal is to expose potential new leaders to experiential challenges and opportunities to build future leadership. It is a competency-based program designed to support GIPSA's succession planning by preparing selected high-potential employees for future supervisory, managerial, and senior technician positions within the Agency through building and improving needed skills, as well as applying new approaches to address present and future needs. This program supports the GIPSA Strategic Plan's Management Initiative 1: Human Capital Management, which states, "GIPSA's Human Capital Plan integrates strategic alignment and planning with workforce development tied to succession planning."

The 12-month program focuses on GIPSA leadership competencies. The program provides the processes, structure, and opportunity for participants to assess their individual leadership developmental needs, plan learning activities, practice and improve leadership skills, explore the dimensions of leadership with experts and colleagues, learn skills they can use now and in the future, and build networks for future collaboration.

The LDP is designed for those who aspire to be in leadership positions and to improve leadership skills needed to succeed. P&SP has had 19 future leaders participate in this program. Seven entered the LDP program in 2010. The participants were required to do a shadow assignment for a week with a current senior leader. Some examples of positions shadowed included the Senior Economist and Assistant to the Deputy Director for Surveillance, Division of Market Oversight of the Commodity Futures Trading Commission, multiple Assistant Regional Inspectors General in USDA's Office of the Inspector General, the Deputy Administrator for P&SP, an Assistant Regional Manager of the Plant Protection and Quarantine program in USDA's Animal and Plant Health Inspection Service, and Director of Department of Initiatives and International Affairs for FGIS.

Packers and Stockyards Automated Software (PAS) Enhancements

PAS has been implemented in multi-year phases due to the extensive work involved in developing an automated system of this nature. To date the system is about 95 percent completed, with only one initial phase awaiting implementation. Enhancements have been implemented simultaneously and separately from various phases of the project. These enhancements have been needed to update previously released phases, improve features within the system, and revise the system due to changes in program procedures and regulations.

Recent enhancements included improved search capabilities and data entry reinforcements for regulatory actions and investigations to reduce the incidence of missing data.

P&SP management fully supports maintenance of the system and allocates funding for continual improvement of the system which will benefit the agency and the users of the system.

This section contains three annual assessments requested by Congress of the entities that P&SP regulates. First, the section provides an assessment of the general economic state of the regulated industries, including trends in the number of firms, financial conditions, and the percentage of the market held by the four largest firms of a particular sector (market concentration).[1] Second, it examines changing business practices of firms in the regulated industries, including pricing methods, and particularly pricing on live weight versus carcass weight; procurement methods, with a focus on commitments to procure more than 14 days before slaughter versus transactions conducted on a cash-carry or spot basis; and trends related to the volume marketed through market agencies via commissions versus direct purchases. Finally, this section outlines specific concerns about the behavior or conduct of the entities regulated under the P&S Act and P&SP's actions to address those concerns.

The number of entities subject to the P&S Act continues to trend downward. As firms exit without replacement, there is a tendency for the larger firms to increase their share of the market as overall volume increases. The decline is greatest in number of bonded packers, with less than 50 percent as many in 2010 as in 2001. Bonded dealers show the least decline, with over 95 percent as many in 2010 as in 2001.[2]

The four largest slaughter firms' share of the total value of livestock purchases (i.e., aggregate industry concentration) increased from about 68 percent in 2008 to 70 percent in 2009. Patterns of concentration in the purchase of different types of livestock, however, have exhibited varying trends.

Concentration in poultry slaughter has trended upward since 2000, whereas four-firm concentration ratios by volume of steer and heifer slaughter and beef production have been relatively stable in recent years. Cow and bull slaughter concentration increased from 1999 to 2007 then declined in 2008 and again in 2009.

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[1] Data in this section is generally from regulated industry annual reports to P&SP, and those reports for the 2010 reporting year are not due until April 15, 2011. Hence most statistics in this section are for 2009. Exceptions are statistics on firms currently bonded and/or registered as recorded in P&SP databases, and market share (concentration) statistics. The latter are based on calendar year federally-inspected slaughter for all but 1980 and for beef production, which are based on firms' fiscal years as reported to P&SP.

[2] Note that not all firms in existence in 2010 would necessarily be among those existing in 2001. The dealer category is especially subject to relatively easy entrance and exit.

Concentration in hog slaughter increased sharply in 2003, declined in 2006, increased in 2007 and remained steady in 2008, with a small decline in 2009. Concentration in sheep slaughter declined in the first half of the decade then increased in 2005 and has remained steady since then.

In general, increases in industry concentration from declining firm numbers reflect efforts by firms to increase net incomes. Agriculture firms in particular have tended to focus on cost minimization to increase net incomes. To achieve this objective, firms have adopted cost-saving technologies (frequently replacing labor with machines) that fostered larger capacities. Low interest rates throughout 2010 have provided additional incentives for firms to replace labor with capital assets. At the processor level increased worker productivity appears to be responsible in part for better income margins.

Some business practice trends are stabilizing. For example, carcass-basis purchases of cattle were 20 million head in 2009 with a 10 year average of 19 million. Carcass based purchases of hogs were 87 million in 2009 with a 10 year average of 79 million. Carcass-based purchases reflect a trend by packers to pay livestock sellers for quality or grade characteristics tied to product values using through contractual arrangements.

Carcass-basis pricing tends to correlate with trends in increased contracting for procurement and reductions in the volume of transactions through market agencies. These trends started over 10 years ago in the livestock/meat sector and will be resistant to change, even in the face of economically stressful conditions since they are related to cost-saving motives for increased coordination of livestock, poultry, and meat production and marketing.

The use of committed procurement methods by the largest beef packers increased in 2009 but the rate of increase continued to decline, continuing a pattern exhibited since 2006. The gain in 2009 came primarily from an increased use of packer feeding; as forward contracts increased slightly and marketing agreements declined. Packer feeding and forward contracting represent only about 12 percent and 10 percent, respectively, of total cattle procurement.

Unlike the livestock industry, which relies on contract procurement to coordinate the market supply channel, the poultry industry has been almost completely vertically integrated for several decades. As a result, the use of spot markets for poultry is virtually nonexistent.

At the end of 2010, 233 bonded livestock slaughter firms, 117 live poultry dealers, 4,468 registered dealers, and 1,205 market agencies were subject to the P&S Act (Table 14). Entities subject to the Act are:

- Bonded slaughter firms include firms operating Federally inspected plants as well as some firms operating plants that are not Federally inspected. Some firms with smaller volume purchases voluntarily bond but do not file annual reports. All packers operating in interstate commerce are subject to the P&S Act, which requires firms that purchase $500,000 or more of livestock for slaughter to be bonded and to file annual reports.
- Livestock dealers purchase livestock for resale on their own accounts and take title to the animals. They may also purchase or sell as the agent or vendor of another entity.
- Market agencies are entities engaged in the business of buying or selling livestock in commerce on a commission basis, furnishing stockyard services, or, in rare cases, an entity providing State brand inspection services.
- Live poultry dealers, commonly called poultry integrators, contract with producers for grower services to raise chicks to slaughter size and weight. The integrator slaughters and further processes the poultry.
- Posted stockyards are physical facilities and are not necessarily separate businesses. For example, a county fairground may be registered as a posted stockyard. Terminal market agencies and auction market agencies are located at posted stockyards, but may or may not be the same entities that own and operate the stockyards.

Table 14. Number of Slaughterers, Live Poultry Dealers, Bonded Dealers, Bonded Market Agencies, and Posted Stockyards Subject to the P&S Act, 2000 - 2010

Year	Bonded slaughter firms	Live poultry dealers	Bonded dealers	Bonded market agencies	Posted stockyards
2000	359	N/A	4,772	1,608	1,519
2001	338	N/A	4,675	1,575	1,525
2002	335	N/A	4,480	1,544	1,510
2003	338	N/A	4,675	1,575	1,429
2004	314	N/A	4,152	1,457	1,443
2005	312	N/A	4,100	1,447	1,426
2006	304	N/A	3,984	1,433	1,400
2007	296	N/A	3,883	1,410	1,413
2008	281	126	4,685	1,326	1,392
2009	284	125	4,529	1,225	1,170
2010	233	117	4,468	1,205	1,209

In 2008, P&SP began transitioning from multiple older databases to a new single database. In the process, data was manually re-entered into the new system after field verification, except for information about posted stockyards, which do not report annually. In 2008, P&SP re-posted 864 known stockyards and in 2009 began de-posting any stockyards that do not respond to a request seeking applicants for re-posting. P&SP did not maintain statistics on live poultry dealers prior to 2008.

The volume of business of packers has trended upward until 2009, then showed a decline returning to 2006 levels. Dollar volume fell to pre-2003 levels for firms selling on commission and for firms operating as dealers or purchasing on commission basis (Figure 10).

The value of bonds held by packers increased in 2009 in spite of the decline in volume of business, but other types of entities show a decline in value of bonds as compared to 2008 (Figure 11). The total value of bonds held by subject firms should continue to follow the same trend as the total dollar business volume of these firms.

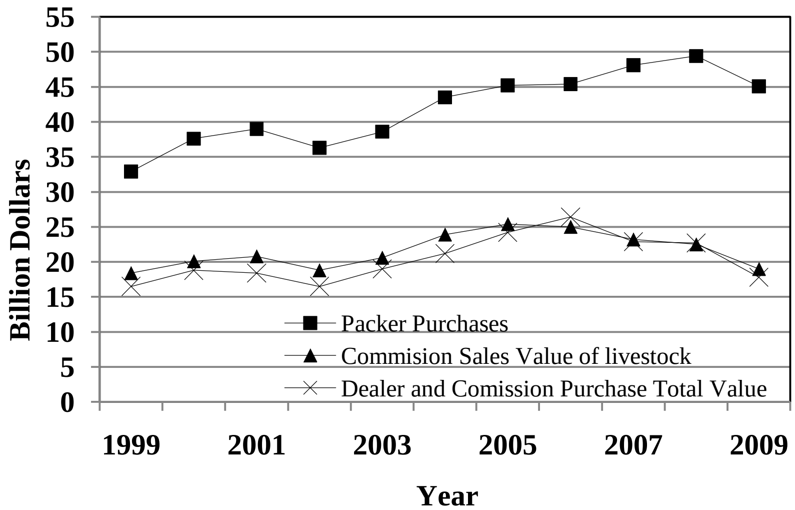

Figure 10. Dollar Volume of Slaughter Firms, Dealers, and Market Agencies Selling and Buying on Commission Subject to P&S Act, 1999-2009

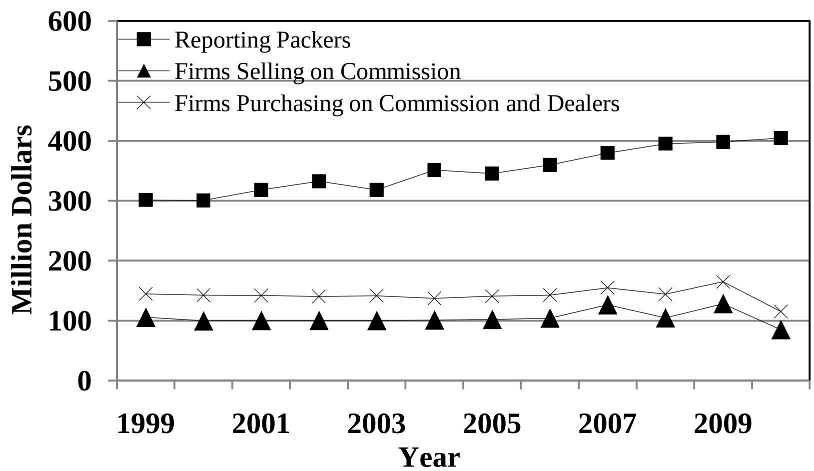

Figure 11. Value of Bonds Held in Accordance With P&S Act by Slaughter Firms, Market Agencies Selling on Commission, and Dealers and Market Agencies Purchasing on Commission, 1999-2009

The four largest slaughter firms' share of total industry expenditures on livestock for slaughter increased in 2009 to about 70 percent (Figure 12).

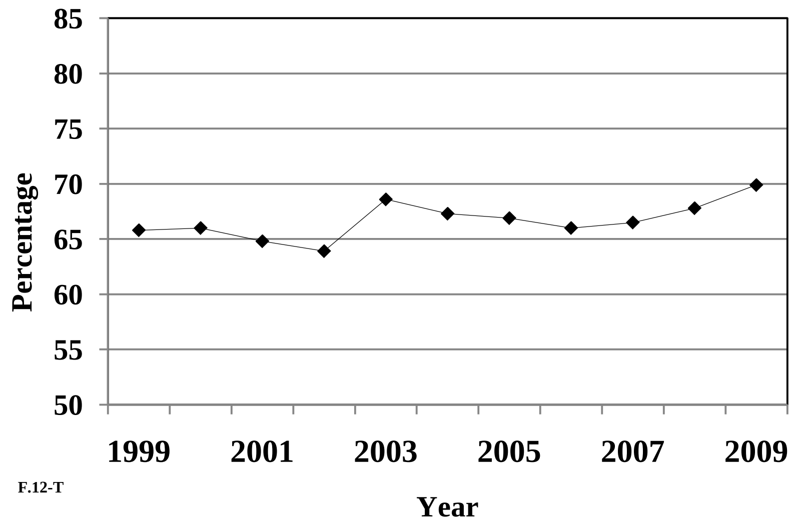

Figure 12. Share of Total Industry Livestock Procurement Expenditures for the Four Largest Slaughter Firms, Ranked by Total Livestock Procurement Expenditure, 1999-2009

While slaughtering and beef processing concentration has generally remained steady since 1995, firms slaughtering hogs have generally increased their market share (Table 15).

Table 15. Four-Firm Concentration in Livestock Slaughter by Type of Livestock and in Fed Beef Production, Selected Years, 1980-2009

Year	Steers & Heifers (%)	Sheep & Lambs (%)	Hogs (%)
1980	36	56	34
1995	81	72	46
2000	81	67	56
2001	80	66	57
2002	79	65	55
2003	80	65	64
2004	79	65	64
2005	80	70	64
2006	81	68	61
2007	80	70	65
2008	79	70	65
2009	81	70	63

Concentration of the four largest steer and heifer slaughterers rose from 36 percent in 1980 to a high of 82 percent in 1994 and has remained relatively stable since then. Four-firm concentration in hog slaughter rose from about 34 percent in 1980 to 64 percent in 2003 through 2005, declined to 61 percent in 2006, and then increased to 65 percent in 2007 and 2008. 2009 posted a decline of two percent in four- firm concentration of hog slaughter. Four-firm concentration in sheep and lamb slaughter rose from 56 percent in 1980 to 73 percent in 1996, but has declined over the last 10 years. Four-firm concentration for Sheep and Lamb slaughter has remained relatively stable since 2007 at 70 percent and continuing the trend through 2009.

Table 16 reports two financial ratios that summarize financial conditions in the meat-packing industry. The *Operating Profit Margin*, computed as operating income (gross profit minus operating expenses) expressed as a percent of total revenue, measures the percentage of revenue from sales that remains after production costs have been paid. It reflects the financial performance or operating efficiency of a company over time or compared to other companies in the same industry. The *Current Ratio* is the ratio of current assets to current liabilities and is a measure of a firm's liquidity or financial health. It indicates the extent to which a company is able to cover its short-term liabilities. For example, a current ratio of 2 indicates that a company's current assets (cash, inventory, and receivables) are twice the value of its current liabilities (debt and payables).

Table 16. Average Operating Profit Margin and Current Ratios for the Top 4 and the Top 20 Firms, 2006 - 2009

	Operating Profit Margin (pct of revenue)		Current Ratio	
Year	Top 4	Top 20	Top 4	Top 20
2006	-0.2	0.8	1.9	1.3
2007	1.0	1.7	1.9	1.6
2008	1.0	2.0	2.9	1.9
2009	2.0	2.0	3.5	2.3

Operating profit margins increased slightly for the 4 largest firms and were unchanged for the 20 largest firms in 2009. The Current ratios for the largest 4 firms and group of 20 largest firms increased in 2009 and also improved across the entire group of 20 largest firms.

These financial data are averaged across a wide variety of types of firms. The size rankings are based on total livestock procurement expenditures. There are differences both across and within size groups in combinations of species slaughtered (beef, pork, sheep, and poultry) by the included firms. Within beef slaughter firms, the larger packers all slaughter a large proportion of steers and heifers in their total slaughter mix. Many smaller packers specialize in cow and bull slaughter and almost no steers and heifers.

Financial data reported to P&SP by some firms may include information on operations other than meat packing and processing. Variation in other types of non-meat activities included in the data from some firms occasionally leads to large swings in some of the ratios, especially for the group of smaller firms.

Cattle -- General Economic State of the Industry

The volume of cattle slaughtered by firms reporting to P&SP (firms with livestock purchases equal to or exceeding $500,000 per year) fluctuates with the cattle cycle. Total cattle slaughter by firms reporting to P&SP trended downward from 2000 through 2005 and resumed that trend in 2008 and has remained relatively constant in 2009 (Figure 13). Total cattle includes steers and heifers (often collectively called “fed cattle”), cows, and bulls. In most but not all cases, individual plants operated by firms that report to P&SP tend to slaughter either fed cattle or cows and bulls.

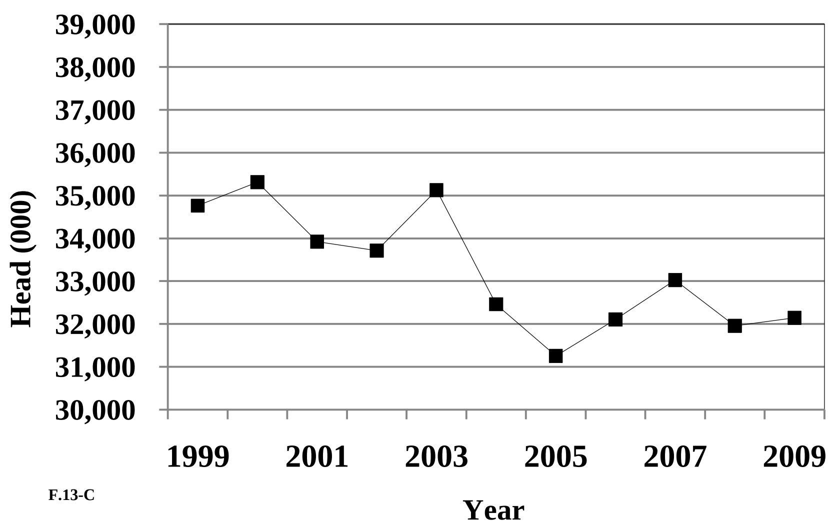

Figure 13. Total Slaughter Cattle Purchases for Firms Reporting to P&SP, 1999-2009

The number of cattle slaughter plants reporting to P&SP declined by approximately 60, or 27 percent, from 1998 through 2003, as plant sizes increased and smaller plants closed (Figure 14). The number of slaughter plants continued to decline in 2009 by an additional 33 compared to 2008. This gradual reduction in total numbers is expected to continue as financial conditions make larger firms look for ways to reduce costs and operate more efficiently.

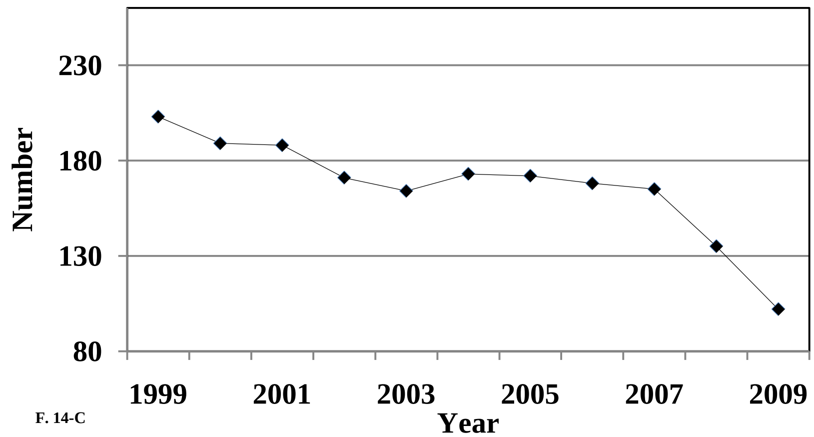

Figure 14. Number of Cattle Slaughter Plants for Firms Reporting to P&SP, 1999-2009

The percentage of the total volume of steer and heifer purchases accounted for by the four largest firms that slaughter steers and heifers has remained between 78 and 82 percent since 1998 (Figure 15).

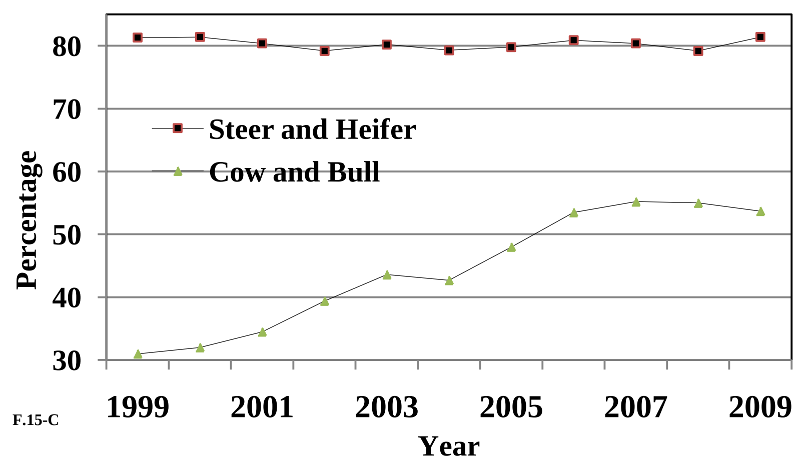

Figure 15. Combined Market Share for the Four Largest Steer and Heifer Slaughter Firms, Four Largest Cow and Bull Slaughter Firms.

Concentration in cow and bull slaughter has always been less than fed-cattle slaughter concentration, but has trended upward since 1999. In 2006, several smaller packers ceased operating and some smaller plants were acquired by larger firms. These factors resulted in an increase in the combined market share of the four largest firms slaughtering cows and bulls.

Future changes in concentration are expected to follow the patterns of the last 5 years, subject to possible changes due to uncertainties about developments in the overall economy that began in 2008.

Hogs—General Economic State of the Industry

The volume of hogs slaughtered by firms reporting to P&SP has trended upward in the last 10 years, partly on the strength of export markets (Figure 16). Total purchases for slaughter are expected to become stable or possibly increase as larger export markets strengthen their own domestic markets and the continued reduction in the breeding herd.

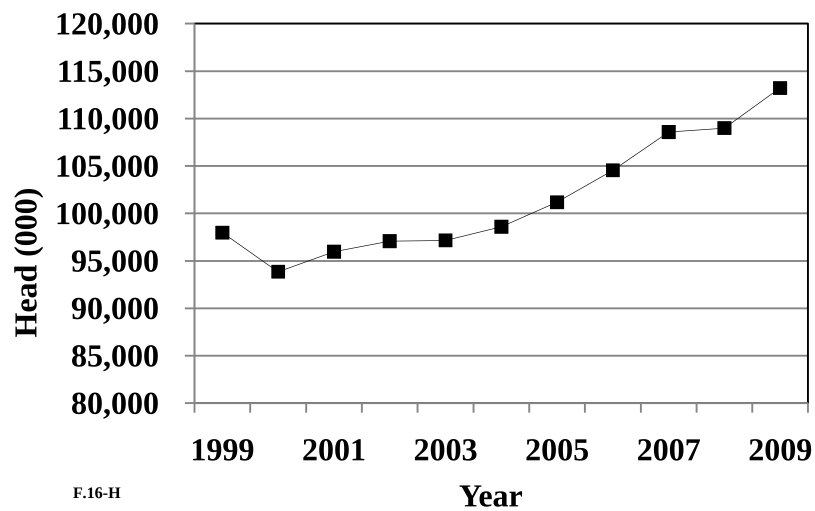

Figure 16. Total Hog Purchases for Slaughter for Firms Reporting to P&SP, 1999 - 2009

The number of hog slaughter plants had been somewhat stable since 2004. In 2008, economic conditions, mergers and acquisitions, and efforts to approve efficiencies resulted in a large decline in the number of plants which continued into 2009 (Figure 17).

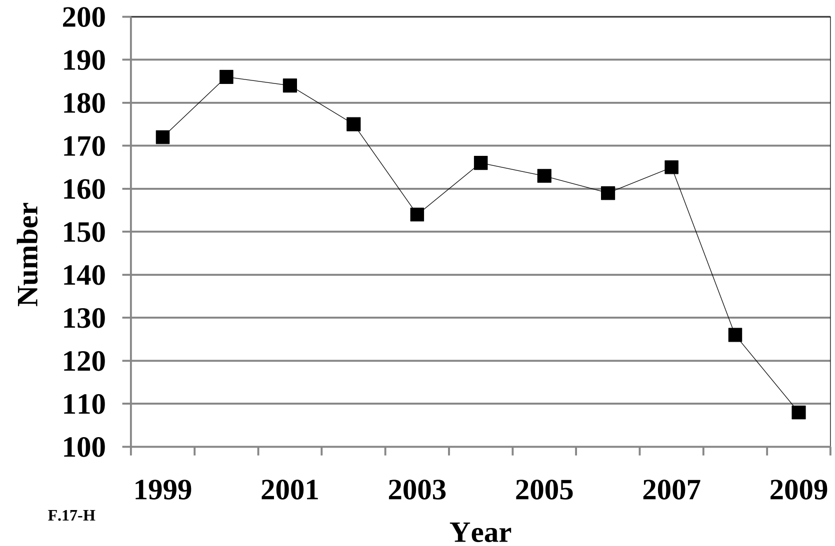

Figure 17. Number of Hog Slaughter Plants for Firms Reporting to P&SP, 1999-2009

The four-firm concentration ratio for hog slaughterers was roughly 56 percent in the late 1990s and then increased to near 65 percent in 2003, where it remained in the mid 60's range through 2009 (Figure 18).

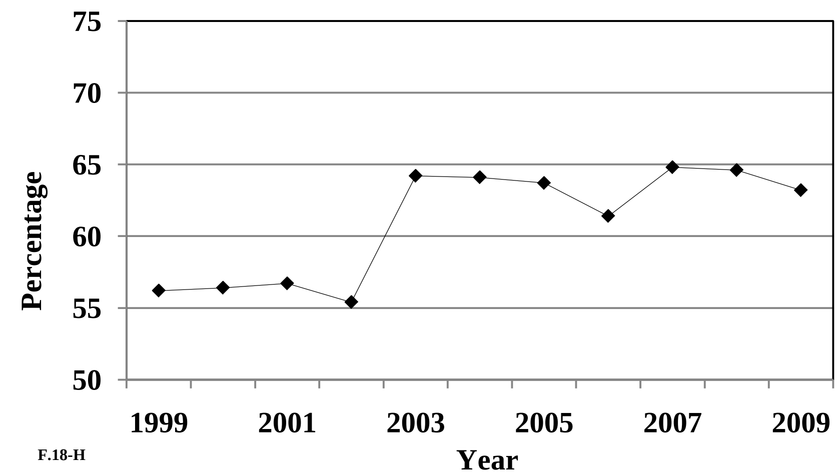

Figure 18. Combined Market Share for the Four Largest Hog Slaughter Firms, 1999-2009

Sheep—General Economic State of the Industry

The volume of sheep and lambs slaughtered by packers reporting to P&SP declined in every year but three between 1998 and 2007, with the sharpest single year decline between 2007 and 2008. The 2009 volume posted a small rebound compared to 2008 (Figure

19). Annual slaughter of sheep and lambs increased from 1.9 million head in 2008 to 2 million in 2009.

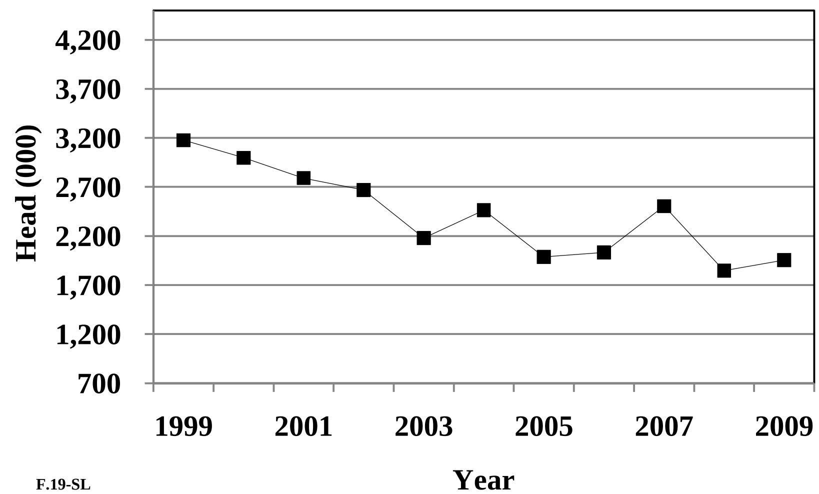

Figure 19. Total Slaughter Sheep and Lamb Purchases for Firms Reporting to P&SP, 1999-2009

The number of plants slaughtering sheep and lambs declined steadily from 1997 through 2002, remained relatively constant through 2007, and declined sharply in 2009. Slaughter plant numbers are expected to continue at present levels in the short term (Figure 20).

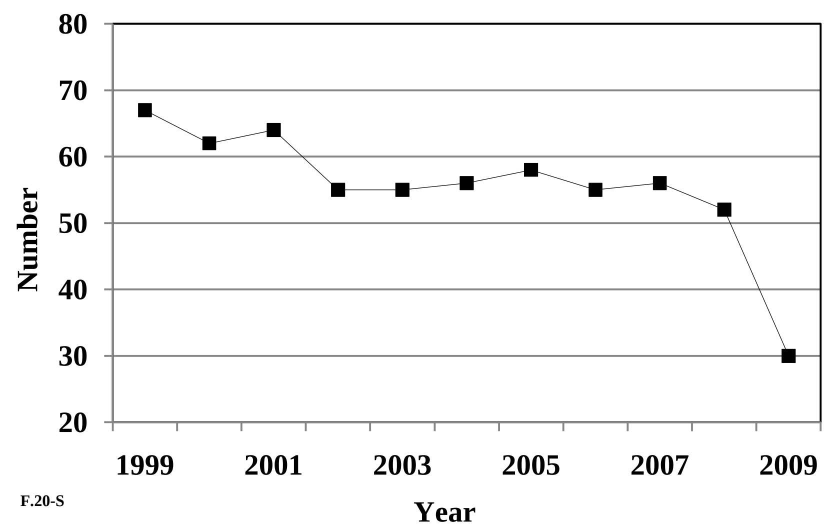

Figure 20. Number of Sheep and Lamb Slaughter Plants for Firms Reporting to P&SP, 1999-2009

The combined market share of the four largest sheep and lamb slaughter firms trended steadily downward from 1998 through 2004, as the largest plants in the industry decreased slaughter faster than total industry slaughter declined (Figure 21).

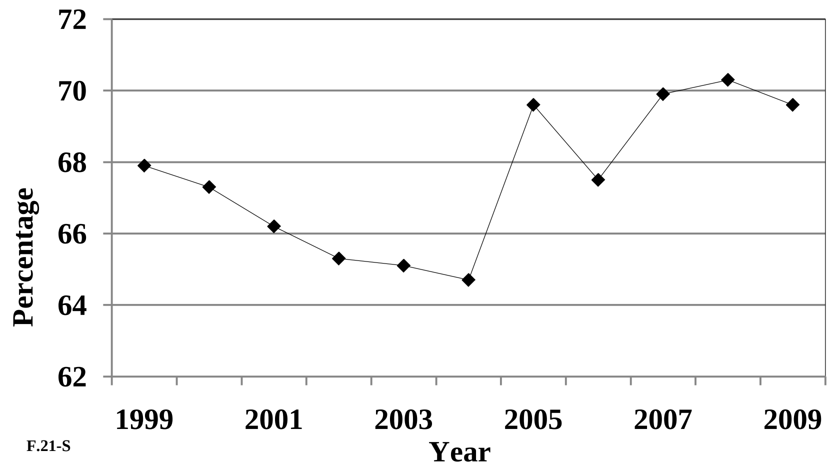

Figure 21. Combined Market Share for the Four Largest Sheep and Lamb Slaughter Firms, 1999-2009

Due to the small total slaughter volume of the industry, relatively moderate volume adjustments by any of the largest four firms result in relatively large changes in the percent of total industry slaughter accounted for by those firms. The long-term decline in share reversed in 2005, when one of the four largest firms exited and the remaining three large firms increased their combined volume by an amount equal to the output of the exiting firm. An additional firm then entered the group of four largest, causing a net increase in total slaughter of the four largest firms and in their share of total industry slaughter.

The share of the four largest lamb packers declined in 2006, returned to 2005 levels in 2007, and decreased slightly in 2009. But, as in previous years, these changes in shares represented only a few thousand head of slaughter lambs. Future changes in sheep slaughter concentration will continue to be variable due to adjustments among the four largest firms, but will likely remain in the 65-70 percent range.

Poultry—General Economic State of the Industry

This section addresses slaughter volume, industry concentration, and two measures of live poultry dealer financial health (the net profit margin and current ratio) obtained from annual reports filed by the industry with P&SP.

In 2009, poultry processors reported to P&SP that they slaughtered 46.4 billion pounds of poultry. By comparison, in 2008, the Federally inspected (FI) volume was 46.2 billion pounds. This continues to reflect an upward trend in poultry slaughter since 1996, when FI volume was approximately 26 billion pounds. Turkey slaughter, in contrast, increased only slightly during the last 10 years, and declined modestly from 2008 to 2009, with firms reporting 6.9 billion pounds to P&SP for 2009 compared to the FI volume of 7.4 billion pounds for 2008. Poultry slaughter volume remained relatively high in early 2008, but slowed considerably in late summer and beyond, triggered by the negative effect of the strong U.S. dollar on exports.

Concentration in broiler and turkey slaughter has trended upwards since 2000. In 2009, the four largest broiler slaughterers posted a 4 percent decline to 53 percent of the market share compared to 57 percent in 2008. The four largest turkey slaughterers posted a noticeable increase of 9 percent to control of 58 percent of the market share in comparison to 2008 at 51 percent. Concentration is expected to remain relatively stable at 2008 levels into 2010.

In 2008, the operating profit margin (the percentage of revenue from sales that remains after production costs have been paid) of the 20 largest broiler companies averaged a negative 1.2 percent, foretelling the coming bankruptcy of Pilgrim's Pride, Inc. However, in 2009 the outcome improved with a positive profit margin of 1.3 percent (Table 17). Profits for the four largest broiler firms averaged considerably lower than profits for the entire group of 20 largest broiler firms. The profit margin for the 20 largest turkey processing companies averaged a negative 1.6 percent profit margin compared to 2008 at with a positive 2.4 profit margin (Table 17). By comparison, the average profit margins of the four largest turkey firms were positive in 2009.

Table 17. Poultry Industry Market Share, Operating Profit Margin, and Current Ratio, 2008 - 2009

Type	Market	Operating Profit Margin (pct of revenue)		Current Ratio	
	Share %	Top 4	Top 20	Top 4	Top 20
Broiler 08	57	-5.4	-1.2	1.9	2.1
Broiler 09	53	0.04	1.3	2.4	2.2
Turkey 08	51	1.8	2.4	1.8	2.4
Turkey 09	58	1.8	-1.6	2.0	2.5

The largest four turkey firms continued to show a lower average liquidity ratio than the group of the 20 largest, whereas the four largest broiler firms had a higher average liquidity ratio than the group of the 20 largest.

The long-term decline in the number of livestock slaughter firms reporting to P&SP reported in the previous section has been accompanied by a trend toward increased specialization in slaughter. This has been illustrated by a greater decline from 1997 through 2006 in the number of firms slaughtering two or more classes of livestock than in the number of firms slaughtering a single class (Figure 22).

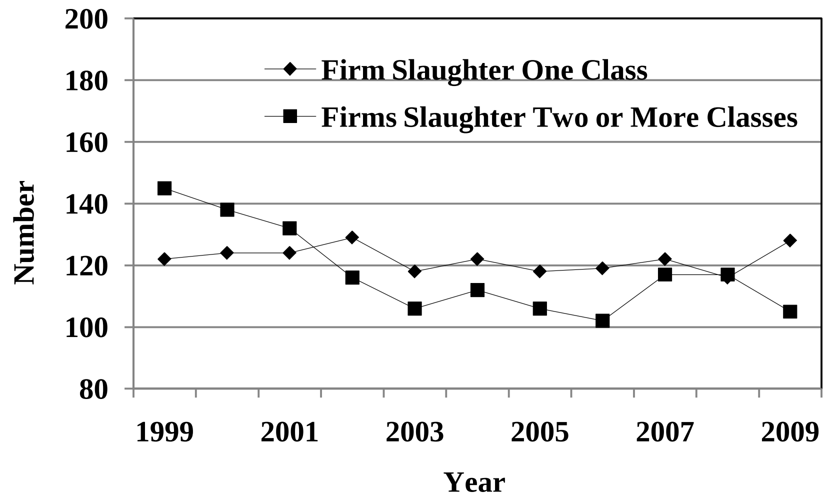

Figure 22. Number of Firms Slaughtering One Class and Number of Firms Slaughtering Two or More Classes of Livestock, 1999-2009.

For purposes of this comparison, the separate classes of livestock are steers and heifers; cows and bulls; calves; sheep and lambs; and hogs. While the number slaughtering two or more classes increased in 2007, it declined in 2009 as the number slaughtering only one class increased.

Cattle—Changing Business Practices

The pricing method that sellers and purchasers agree to use for a transaction is a fundamental characteristic of any market transaction. For livestock and for cattle transactions in particular, pricing methods are most often divided into two categories: live-weight and carcass pricing methods.

In live-weight purchasing of livestock, the price is quoted and the final payment is determined based on the weight of the live animal. Transactions that use some variation of live-weight purchasing are usually on an "as-is" basis with a single price per pound for all animals in the entire transaction.

The price may be fixed by negotiation in advance, or established from prices reported by a market price reporting service after the animals are delivered or slaughtered. In some instances, provisions may be made for paying different prices for animals that differ significantly from other animals in the transaction (e.g., animals that are much smaller than the average for the transaction may receive a lower price).

In a "carcass-based" purchase, the price is quoted and the final payment is determined based on each animal's hot weight, which is the weight of the carcass after it has been slaughtered and eviscerated.

Carcass-based purchase methods often involve schedules of premiums or discounts based on animal quality and other features, such as time of delivery and number of animals in the transaction. The price before premiums or discounts is referred to as the "target" or "base" price. Carcass-based pricing typically rewards sellers with livestock that meet or exceed the target standard. Livestock carcasses graded below the target result in the seller receiving significant discounts.

After declining annually through the 1990s, the proportion of cattle purchased on a live-weight basis by packers reporting to P&SP had been uneven but continued to remain nearly constant in 2009 compared to 2008 (Table 18).

Table 18. Number and Percentage of Cattle Purchased Live-Weight and Carcass-Weight by Packers Reporting to P&SP, 1999-2009

	Live-weight		Carcass-weight	
Year	Head (000)	Percent	Head (000)	Percent
1999	17,546	50.5	17,217	49.5
2000	17,102	48.4	18,207	51.6
2001	15,044	44.3	18,877	55.7
2002	12,555	37.2	21,158	62.8
2003	14,116	40.2	21,008	59.8
2004	15,112	46.6	17,348	53.4
2005	13,663	43.7	17,591	56.3
2006	15,004	46.7	17,012	53.3
2007	14,135	42.8	18,887	57.2
2008	12,043	37.7	19,916	62.3
2009	12,282	38.2	19,863	61.8

The total volume of cattle purchased on a carcass basis trended upward from 1998 through 2002 (Figure 23). Following a sharp decline in 2004, the volume stabilized in 2005 and 2006, and then increased through 2008 remaining close to constant in 2009. The proportion of cattle purchased on a carcass basis is expected to remain in the 60-percent range with modest fluctuation year over year.

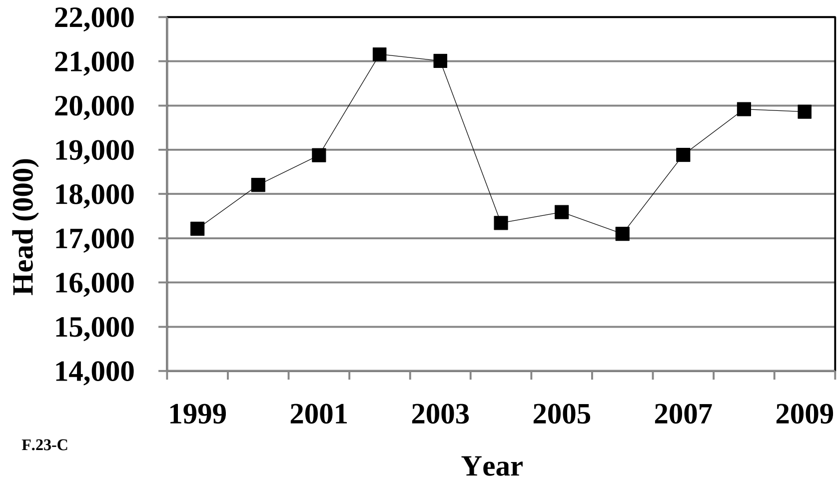

Figure 23. Cattle Purchases on a Carcass Basis, 1999-2009

The proportion of calves purchased on a carcass-weight basis was considerably less and at the lowest point since 1999 for 2009, but has exhibited a mixed pattern in recent years. After declining from 2000 through 2003, the proportion of calves purchased on a carcass basis increased almost 10 percentage points in 2004, reversed and decreased sharply in 2005, trended up in 2007 and 2008, then decreased once again in 2009 (Table 19).

Table 19. Number and Percentage of Calves Purchased Live-Weight and Carcass-Weight by Packers Reporting to P&SP, 1999-2009

	Live-weight		Carcass-weight	
Year	Head (000)	Percent	Head (000)	Percent
1999	504	47.6	556	52.4
2000	495	51.3	470	48.7
2001	479	54.7	397	45.3
2002	492	57.3	367	42.7
2003	553	59.4	377	40.6
2004	351	49.6	357	50.4
2005	415	63.7	236	36.3
2006	397	66.3	201	33.7
2007	387	61.1	247	38.9
2008	338	53.9	289	46.1
2009	454	72.5	172	27.5

Packers have increased the development and testing of carcass evaluation devices in the beef industry. P&SP participates in carcass tests conducted jointly by USDA's Agricultural Marketing

Service (AMS) and evaluation-device manufacturers to test device performance under real-time conditions in packing plants. While these devices are not yet being used as a basis for payment to producers, the industry is poised to augment traditional AMS meat-grading services with complex images that provide a “score” of carcasses for both yield grade and marbling.

Another business practice affecting transactions involves the location in the market channel of the transaction. P&SP monitors two major transaction location points in livestock marketing. One major transaction point is exchange between the livestock producer and an assembly point, usually a market that accepts the livestock on a commission basis. The buyer procures the livestock through the market, generally with no direct contact between seller and buyer.

Although the volume of cattle handled by commission firms has declined over the last 10 years, these firms continue to play an important role in the cattle industry, particularly for cull cows (Figure 24).

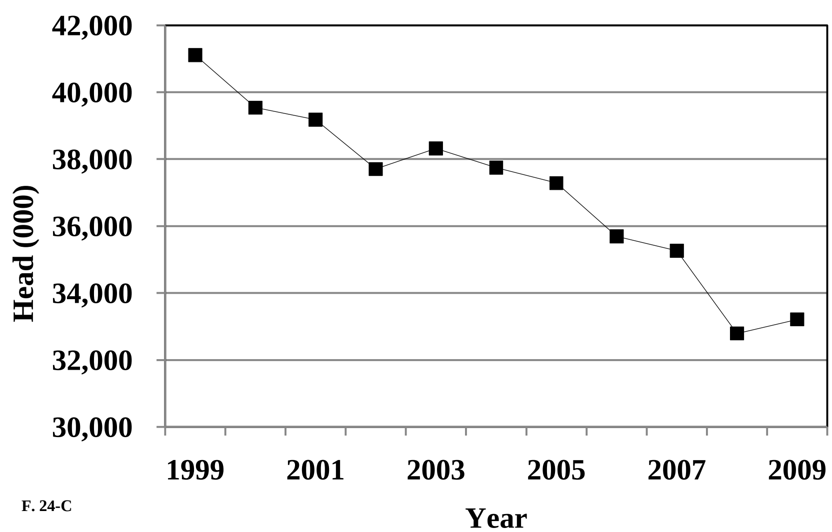

Figure 24. Volume of Cattle (Slaughter and Non-Slaughter) Marketed Through Firms Selling on Commission, 1999-2009

The second transaction location point monitored by P&SP is direct exchange between the livestock seller and the packer. Packers use multiple direct exchange procurement methods to obtain live cattle for slaughter. The methods commonly fall into two categories: (1) cash or “spot” sales for immediate delivery or normally delivery within at most 14 days, and (2) “committed procurement” arrangements that create an assured exchange and commit the cattle to a particular packer more than 14 days prior to delivery.

GIPSA's reported measure of committed procurement includes cattle sold under an advanced volume commitment regardless of pricing method or the timing of price determination. AMS publishes daily prices and volumes of livestock purchased under alternative definitions based on pricing method. For example, AMS's definition of formula cattle is based in part on the price being determined at a future date. Thus, there are some arrangements that GIPSA considers non-committed that fall into the AMS formula purchase type.

One example is "market price" or "top-of-the-market pricing" (TOMP) arrangements. These arrangements are often on-the-spot bids by packers to buy cattle at the current week's average market price or top market price. The sellers decide on a week-to-week basis or even on a lot-by-lot basis whether to sell under those terms, thus there is no long-standing agreement or advance commitment by the seller to deliver cattle to the packer making the bid. However, the price is not determined until the week's trades are completed and the average or top market price has been established. Thus, these arrangements fit the AMS definition for the formula category.

Another example of a difference in the measures relates to how negotiated grids are negotiated. GIPSA considers negotiated grids that establish a set negotiated base price that is known at the time of the agreement to sell in general to be noncommitted purchases as long as the commitment to deliver is made 14 days or less before slaughter. However, negotiated grids that establish a base price via a formula based on a market price to be determined at a later date are classified as committed procurement if the agreement is made more than 14 days before slaughter. The AMS definitions of negotiated grid and formula purchases depend on what is being negotiated. If the base price level is negotiated as a fixed dollar amount, the arrangement would fit the AMS definition of negotiated grid. If the base price is negotiated relative to a market price (for example "market price" plus or minus an adjustment, where the adjustment is the subject of the negotiations), the transaction would fit the definition of a formula purchase, where the base price is determined at a future date.

There are other measurement differences between GIPSA and AMS defined measures of procurement methods in terms of coverage, data sources and timeliness. GIPSA's statistics only cover the top four beef packers (80 percent of fed cattle), while AMS reports for all Federally inspected packers that slaughter

125,000 head of cattle per year. GIPSA uses data provided by packers generated directly by the packers' own information reporting systems while AMS uses specific standardized reporting forms mandated by the Livestock Mandatory Reporting Act, section 911(2) of title IX of the Agriculture, Rural Development, Food and Drug Administration, and Related Agencies Appropriations Act, 2000 (Public Law 106-78). Also, GIPSA reports yearly on a calendar-year basis, by slaughter date (not procurement date) and as a percentage of total slaughter.

Why the definitions matter: The procurement practices covered under GIPSA's definition of committed procurement or AMS nonnegotiated categories are not prohibited by the P&S Act. Nonetheless, it is thought by some that those methods, if widely used, may have the effect of reducing competition in markets for fed cattle.

Some industry observers have long believed that committed procurement methods, sometimes collectively labeled Alternative Marketing Arrangements (AMAs), are used by packers to reduce demand for cattle in the cash market and thereby reduce cash market prices. Some express a belief that AMAs can be used to depress not only cash market prices but cattle prices under all procurement methods. The belief is that potential anticompetitive effects of alternative marketing arrangements are present not because of the volume commitment associated with AMAs, but due to the pricing method or pricing commitment. If a procurement method, such as TOMP reduces the size of the market used to establish the market price (in this case, the negotiated cash market), then the effect is to reduce competition in the market that sets the price regardless of whether the cattle are committed in advance or not.

Stated another way, purchases under any method, where the price is determined by the market price or a plant average procurement price (most formula and TOMP purchases are priced this way), reduce the volume in the cash spot market that establishes those prices. At some point that market could become so thin or dominated by a single buyer that the price is not a competitive price, but a monopsony or oligopsony price, yet that (presumably lower) price is being used to establish the base price of the formula purchases, futures prices, as well as cash prices. The burden of price discovery is placed on others in the case of formula or TOMP pricing. Those buying and selling under formula or TOMP agreements and not participating in the cash market become "free riders" letting other firms that participate in the cash market establish the price. As that cash market thins, and especially if it comes to be dominated by a single buyer, the probability increases that that cash spot price is not being established in a competitive market and will more likely be lower.

To those that believe this free rider problem is depressing fed cattle prices, the relevant measures to monitor are the volume of the negotiated cash transactions and the number of packers bidding in the negotiated cash market each week.

On the other hand, some believe captive supplies and AMAs lead to improved cattle quality, improved seller certainty and packer efficiency, and greater economic welfare for consumers, packers and producers. According to this set of beliefs, those benefits offset any minor downward price effect that AMAs may have.

From 1999 to 2005, P&SP collected and audited data on the three major committed procurement methods used by the four largest firms that slaughter fed cattle. In 2006 through 2008, P&SP expanded its collection to include data from the five largest fed-cattle slaughter firms, and then resumed collecting from four firms in 2009. The firms use packer feeding, forward contracts, and marketing agreements to procure cattle more than 14 days prior to slaughter, for delayed delivery (Figure 25).

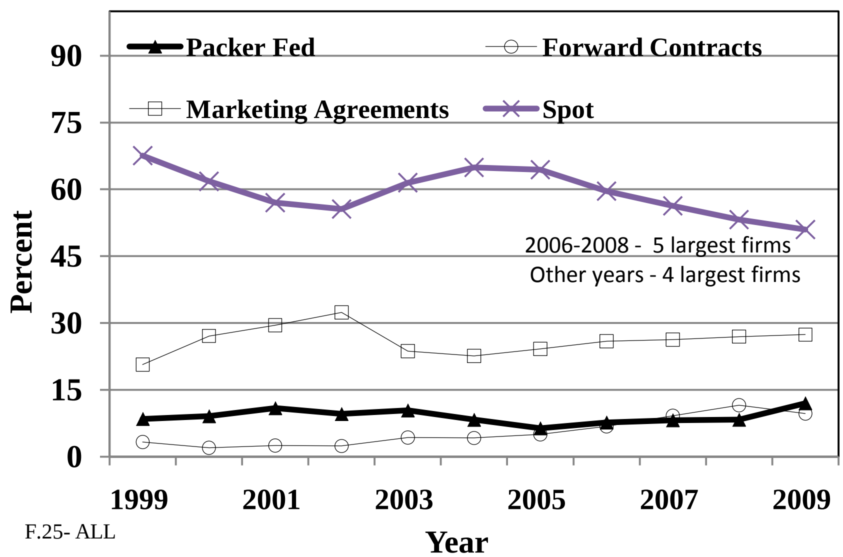

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Figure 25. Types of Procurement Arrangements Used by the Largest Steer and Heifer Slaughter Firms, 1999 - 2009

From 2008 to 2009, total fed cattle slaughter decreased 3.7 percent for the top four beef packers. Overall committed procurement of fed cattle by the top five beef packers increased from 46.8 percent of fed cattle slaughter in 2008 to 49.0 percent of slaughter in 2009. All categories of committed procurement except forward contracts increased in percentage terms from 2008 to 2009. The total increase was 2.2 percentage points, as the rate of increase continued the decline it has exhibited since 2006. The gain in 2009 came primarily from an increased use of packer feeding as forward contracts declined and marketing agreements increased slightly. Packer feeding and forward contracting represent only about 12 percent and 10 percent, respectively, of total cattle procurement.

P&SP defines “packer fed” livestock as all livestock obtained for slaughter that a packer, a subsidiary of the packer, the packer’s parent firm, or a subsidiary of the packer’s parent firm owns, in whole or part, for more than 14 days before the packer slaughters the livestock. The percentage of total purchases of fed cattle that is obtained through packer feeding arrangements by the largest steer and heifer slaughter firms declined in 2004 and 2005. The largest increase by category was Packer Fed and Other, which rose from 8.3 percent of total slaughter in 2008 to 12.0 percent in 2009.

Marketing arrangements termed “forward contracts” are agreements between packers and sellers for deliveries more than 14 days in the future of specific lots or quantities of livestock. The price of the cattle in a forward contract can be set at the time of the contract or determined upon delivery based upon an agreed pricing arrangement. For example, the agreement could use prices from the Chicago Mercantile Exchange futures market for live cattle, with an adjustment for the basis, or expected difference between the futures market price and price in the local area, at the time of delivery. The percentage of fed cattle procured through the use of forward contracts by the group of largest steer and heifer slaughter firms has trended upward since 2004. The only decrease by category for 2009 was Forward Contracts, which fell from 11.6 percent of total slaughter in 2008 to 9.6 percent in 2009.

The term “marketing agreements” includes a variety of arrangements that establish an ongoing relationship for trading multiple lots of cattle rather than negotiating single lots of cattle. In these arrangements, the seller agrees to deliver cattle to the packer at a future date, with the price generally being determined by some type of formula pricing mechanism. The price is often based on the current cash market at the time of delivery, with premiums or discounts determined by evaluation of carcass characteristics. Many producers join together in alliances or cooperatives to commit livestock through one of these agreements.

Of the three categories of committed procurement, marketing agreements account for the largest proportion of total committed procurement. The percentage of fed cattle procured through the use of marketing agreements by the largest steer and heifer slaughter firms fell in 2003 and 2004, and then increased marginally from 27.0 percent of total slaughter in 2008 to 27.4 percent in 2009.

Information about business practices at the plant level, namely level of operations (e.g., one or two shifts per day), number of plants in business at any given time, and ownership of them, is also significant in describing industry trends.

Plant closures or re-openings can have direct competitive effects by shifting supply and demand patterns. The P&S Act does not provide authority to the Secretary for pre-merger review. Rather, that is the responsibility of either the DOJ or Federal Trade Commission under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (Public Law 94-435, known commonly as the HSR Act). Mergers and acquisitions, however, cause changes in business practices that may impact competition. P&SP monitors these industry events for any competitive effects.

The beef packing industry saw considerable activity in 2010. Multinational firm JBS S.A. (JBS) entered into several actions. On February 22, JBS completed its acquisition of Tatiara Meat Company in Australia. Tatiara is a lamb processor. JBS paid 30 million Australian dollars for the firm (http://www.jbs.com.br). In March, JBS announced plans to purchase the assets of Rockdale Beef Partnership in Australia. Rockdale Beef had capacity to slaughter 200,000 head per year and a 50,000 head feedlot. In June, JBS announced plans to purchase McElhaney Feedlot in Welton, Arizona, for $24 million. The feedlot had a one-time capacity of 130,000 head, and was located near JBS's plant in Tolleson, Arizona. On December 28, 2009, JBS finalized its purchase of a controlling interest in Pilgrim's Pride Corp. JBS purchased 64 percent of Pilgrim's voting shares for $800 million in cash. On December 31, 2010, JBS completed its merger with Bertin S.A.

In March~~,~~ 2010, Hastings Acquisitions, LLC purchased the former Premium Protein Products facilities in Hastings, Nebraska and Lincoln, Nebraska for $3.9 million.

In June~~,~~ 2010,Cargill Meat Solutions Corp. and Meyer Natural Angus announced a joint marketing agreement to market Meyer Natural Angus and Laura's Lean Beef to Cargill's customers. Cargill will process the products it markets for Meyer Natural

Angus at Cargill's plant in Fort Morgan, Colorado (http://www.cargill.com).

Hogs—Changing Business Practices

The proportion of hogs purchased on a live-weight basis steadily declined over the past several years; carcass-based purchases have become the predominant method used for hogs purchased for slaughter. The substantial decline in 2009 appears to be a realignment with the normal carcass-based purchase average (Table 20; Figure 26). The proportion of hogs purchased on a carcass basis will likely continue to increase as a total of hog slaughter.

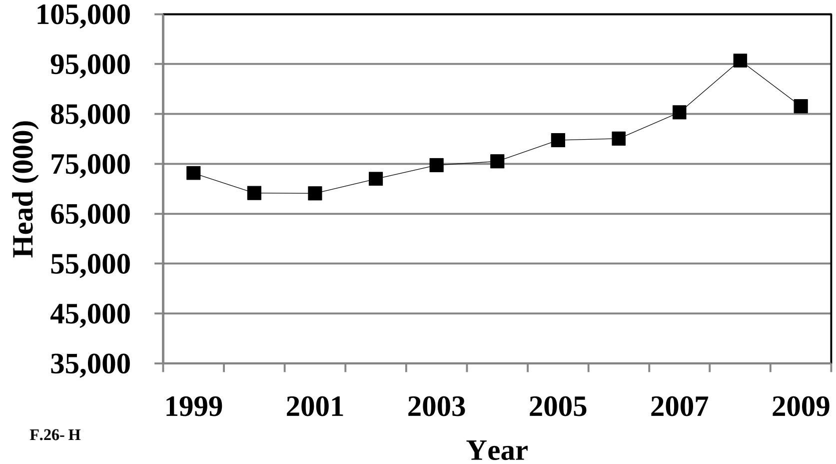

Figure 26. Hog Purchases on a Carcass Basis, 1999-2009

Some carcass-based purchases, often known as “carcass-merit” purchases, include a base price that applies to all carcasses in the transaction, with premiums or discounts for individual carcasses based on quality or other attributes of each carcass, such as quality grade, yield grade, yield, or percentage of lean meat in the carcass. Some carcass merit transactions use USDA grades to determine carcass quality. A growing number of transactions include price adjustments for quality characteristics that are not covered by USDA grades, such as percent of lean meat in the carcass and depth of the loin.

Table 20. Number and Percentage of Hogs Purchased by Live-Weight and Carcass-Weight for Packers Reporting to P&SP, 1999-2009

	Live-weight		Carcass-weight	
Year	Head (000)	Percent	Head (000)	Percent
1999	24,823	25.3	73,153	74.7
2000	24,711	26.3	69,145	73.7
2001	26,883	28.0	69,070	72.0
2002	25,077	25.8	72,003	74.2
2003	22,413	23.1	74,748	76.9
2004	23,092	23.4	75,496	76.6
2005	21,453	21.2	79,730	78.8
2006	24,474	33.4	80,075	76.6
2007	23,238	21.4	85,344	78.6
2008	13,295	12.2	95,708	87.8
2009	26,653	23.5	86,569	76.5

The volume of hogs marketed by firms selling hogs on commission declined between 1999 through 2002. Since 2002, the number has trended steadily upward except for a 1-year decline in 2008 (Figure 27). The decline was reversed as 2009 posted a sharp increase of 1.5 million head. Future changes will likely adjust back to remain close to 7 million head.

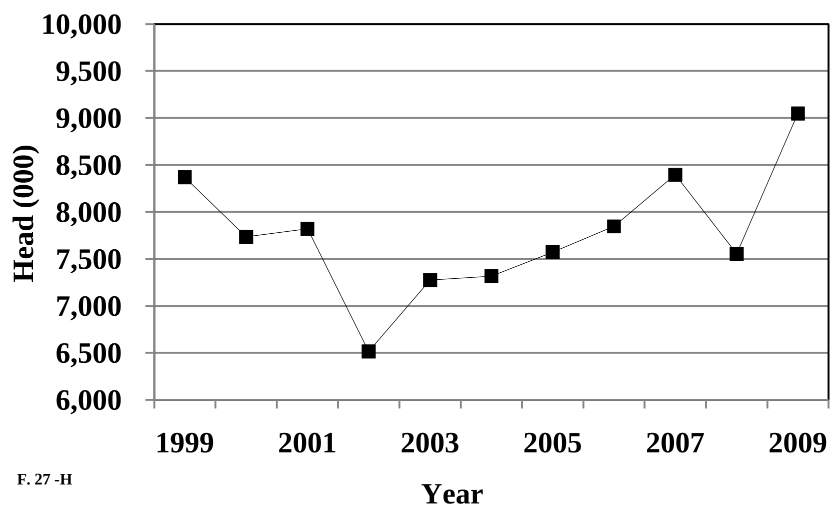

Figure 27. Volume of Hogs Marketed Through Firms Selling on Commission, 1999 - 2009

Like beef packers, pork packers use multiple procurement methods (Figure 28). About 8 percent of hogs were obtained on the negotiated spot market in 2009 compared to 12 percent in 2008. Approximately 22 percent, 1 percentage point more than in 2008, were packer-owned hogs that were supplied from a packer-owned farrowing operation and were often fed under contract for the packer. The rest were purchased using various types of other marketing arrangements, usually either some variation of marketing agreement or forward contract. These agreements increased 2 percentage points compared to 2008. Marketing agreements for hogs generally are based on multi-year contracts under which the producer agrees to deliver a set number of pigs per year to a packer. Some of these arrangements are verbal agreements. “Forward contracts” for hogs are typically simple one-time contracts for a given number of hogs to be delivered within a certain time window, with price based on a futures contract. Other modes of procurement for hogs are largely verbal contracts.

Procurement methods used by individual packers vary significantly among packers, ranging from the packers that are fully integrated to packers that rely primarily on the open market. Most hog packers use some combination of packer-fed hogs, marketing agreements, forward contracts, and negotiated spot market procurement. These combinations typically vary by plant for multi-plant packers.

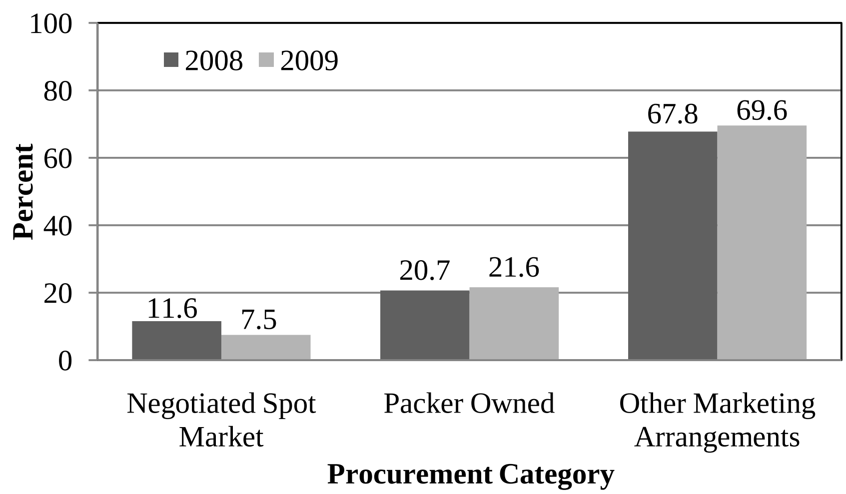

Figure 28. Percentage of Hogs Procured Through Alternative Types of Procurement Arrangements by Four Largest Hog Slaughter Firms, 2008 - 2009

Sow numbers for the largest 25 pork producers dropped less than 1 percent in 2010. Seven of the 25 largest pork producers are hog packers owning about 1,733,204 sows or 60 percent of the amount held by the largest 25 U.S. hog producers. The productivity of the nation’s sow herd had a slight increase reaching an average of 11 pigs weaned per litter with roughly 30 pigs per sow per year. The increased productivity, however, did not offset the drop in herd size.

The daily hog processing capacity dropped slightly in 2010 compared to 2009. John Morrell & Co. (a subsidiary of Smithfield Foods, Inc.) closed its hog processing and fresh meat fabrication plant in Sioux City, Iowa.

Trim-Rite, Carpentersville, Illinois, announced in October, 2010, its intent to purchase the former Meadowbrook Farms pork plant in Rantoul, Illinois. The plant will be known as Rantoul Foods, and it will handle both hog slaughter and pork processing operations with startup projected in April 2011.

Through much of 2010 wholesale pork prices were above 2009 price levels. Through late August, the average 2010 USDA estimated pork carcass cutout[3] was 40 percent above the cutout value for the same period in 2009. In 2010 the July-August average cutout averaged $88.14 or 52 percent above the same period in 2009. While part of the strong increase in the carcass cutout is attributable to lower pork production, domestic consumer demand is likely a significant factor with belly prices being 49 percent higher than in 2009 and loin prices being 27 percent higher than in 2009.

Sheep—Changing Business Practices

The volume of sheep and lambs purchased on a carcass basis peaked at over 1.9 million head in 2001. The trend before 2009 was a decline year over year starting in 2002 and continuing to a sharp decline in 2009 to around 600 thousand head aside from the small gain in 2007 (Figure 29).

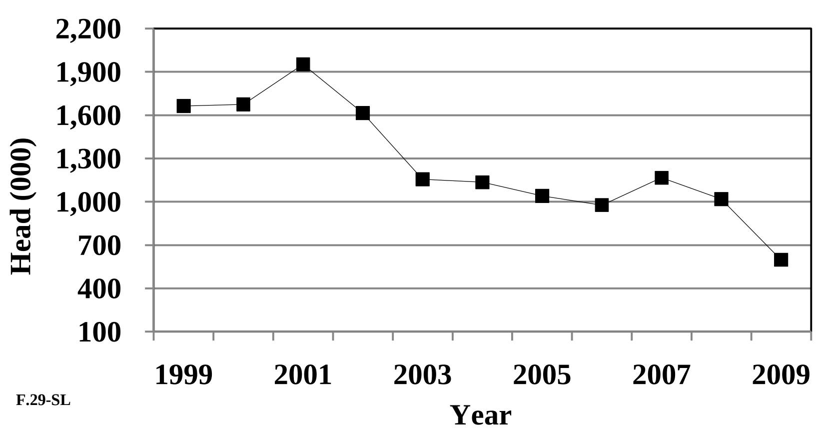

Figure 29. Sheep and Lambs Purchased on a Carcass Basis

[3] Carcass cutout is an estimate of the value of a hog carcass based upon current wholesale prices being paid for cuts that can be taken from the carcass.

The volume of carcass purchases has declined with total slaughter over time, and purchases of sheep and lambs on a carcass basis declined sharply by 20 percent in 2009. Live-weight purchases in 2009 increased substantially to 69 percent of the sheep and lamb purchases for slaughter by packers reporting to P&SP (Table 21).

Table 21. Number and Percentage of Sheep and Lambs Purchased by Live-Weight and Carcass-Weight for Packers Reporting to P&SP, 1999-2009

	Live-weight		Carcass-weight	
Year	Head (000)	Percent	Head (000)	Percent
1999	1,513	47.6	1,663	52.4
2000	1,323	44.1	1,674	55.9
2001	840	30.1	1,951	69.9
2002	1,062	39.6	1,615	60.4
2003	1,023	47.0	1,156	53.0
2004	1,329	53.9	1,135	46.1
2005	948	47.7	1,040	52.3
2006	1,056	51.9	977	48.1
2007	1,338	53.4	1,166	46.6
2008	828	44.8	1,019	55.2
2009	1,357	69.4	598	30.6

Procurement methods used to purchase sheep and lambs for slaughter are similar to those used for other species and include purchase in spot markets, use of marketing agreements, use of various other forms of advance sales contracts, and packer feeding.

Some producers who feed their own lambs market their lambs through a lamb feeding operation or feedlot that has a supply contract agreement with a packer. There also are business arrangements in which individuals who have financial interests in large lamb packing companies also have lamb feeding operations and supply lambs to the packing company. Some producers participate in cooperatives, associations, or pools of lamb producers to collectively market their lambs and lamb products.

As with other species, the various procurement methods used for lambs continue to evolve, but P&SP has not observed major changes in the methods in recent years and expects this stability to continue.

Use of commission firms for the sale of sheep and lambs has declined similarly to the decline in use of commission firms for cattle through 2007. The number of sheep and lambs marketed through commission firms remained steady in 2009 and will likely continue to remain steady in the near term (Figure 30).

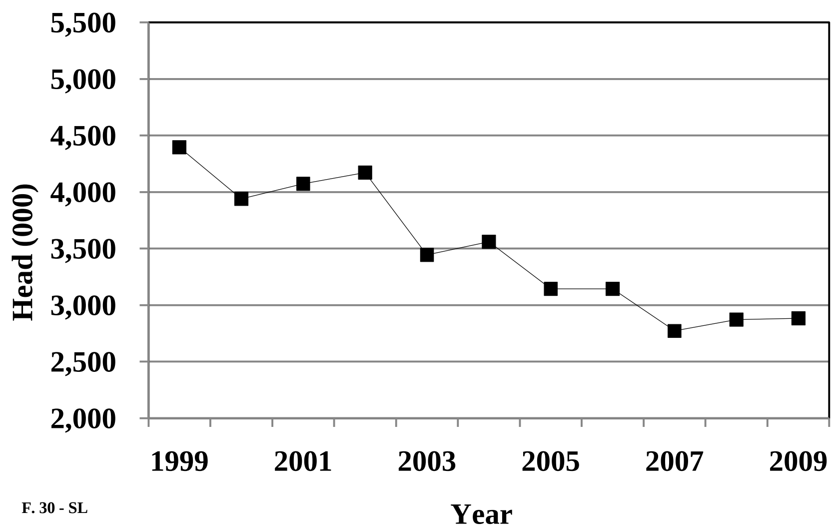

Figure 30. Volume of Sheep Marketed Through Firms Selling on Commission, 1999 - 2009

Poultry—Changing Business Practices

In general, the poultry industry in 2009 rebounded from 2008 and companies gradually increased production through 2010, but recent forecasts for prices of corn and other feed ingredient have lowered 2011 growth and profit expectations.

Pilgrim's Pride came out of bankruptcy almost a year after it filed in December 2008. As a result of the bankruptcy, Pilgrim's Pride closed several plants and reduced production at others, terminating grower contracts at these plants. Pilgrim's is now primarily owned by JBS, but continues to operate as Pilgrim's Pride. It has stated plans to reopen the Douglas, Georgia, complex in 2011, which closed during bankruptcy proceedings.

Foster Farms bought the Pilgrim's complex in Farmerville, Louisiana. Foster was slowly bringing the plant back into production and had contracts with about 100 poultry growers in October 2010, when Foster announced it would delay further expansion and hold production at current levels due to rising feed costs.

Sanderson Farms, Inc. reports it expects to build and open a new broiler complex in North Carolina in the summer of 2012.

Industry Concerns

Markets with self-referenced price determination: The fed cattle markets have shown a relatively large increase in contracted transactions that refer to a negotiated market price for the price used to settle the contract transaction at delivery. For example, GIPSA's top four packer procurement data in 2008 showed the percent of the national negotiated market to be 53 percent and then in 2009 the negotiated market moved to 51 percent. Data from AMS for the Texas-Oklahoma region, which has a large volume of total procurement from large feed lots, was more extreme with 43 percent in the negotiated market in mid-2008 and only 30 percent in mid-2009. The hog markets are even more thinly traded on negotiated markets with GIPSA's top four procurement data also showing a decrease in negotiated market as data in 2008 was 11.6 percent in the negotiated market and only 7.5 percent in 2009. And like fed cattle in the Texas-Oklahoma market, AMS data shows the Iowa-Minnesota market, which has a high proportion of large swine contractors, had only roughly 2 percent of its volume traded in negotiated transactions in mid-2009.

In many of these thinly traded regional markets only a few transactions—and in some cases a single lot transaction—may set the day's negotiated price, which is then referenced to settle thousands of contract transactions easily valued at over hundreds of thousands of dollars. In effect, the price information provided by the negotiated market is a public good that is referenced in contract transactions as a mechanism to lower cost of price discovery. From the economic literature on public goods it is known that public goods are provided at below optimal levels due to the free rider effect, that is, the benefits of negotiating the price do not accrue solely to the person engaged in the negotiated transaction. Supporting this notion, GIPSA continues to receive complaints that these markets with high volumes of self referenced price discovery have distorted supply-demand price determination.

Poultry tournament systems: GIPSA has received an increase in a range of complaints related to price determination in poultry tournament systems. Growers have complained about poultry integrators replacing the growers in a settlement group after settlement and then recalculating the wage rate paid. Another type of complaint is that integrators segregate a subset of a settlement group and make a different management treatment available to the subset, which allegedly affects the remaining group adversely on payment. Another example pertains to settlement calculations, which typically calculate a grower's payment for service provided based on a per-unit cost for chicks and cost of feed provided by the integrator to the grower. These costs typically do not reflect market prices and may or may not be fairly stable across multiple tournaments. Changing one price relative to another will favor or penalize the rankings of a grower based on either feed conversion, if unit feed costs are increased, or chick mortality, if chick costs increase.

These complaints suggest that the grower's ranking in any particular tournament is beyond the control of the grower. By contrast, price determination in competitive markets establishes the value each trader receives from the transaction based on supply-demand conditions outside the control of either trading partner. The determination of the grower's wage rate in any given poultry tournament is highly partial, and equity considerations rest on the benevolence of the integrator in any particular settlement.

Report Provenance

Congress mandated specific content of this P&SP Annual Report with amendments to the P&S Act. Specifically the information on the disposition of cases was mandated by the Food, Conservation, and Energy Act of 2008 (Farm Bill). The relevant amendment in the Farm Bill to the Act states:

SEC. 416. ANNUAL REPORT.

(a) In General.--Not later than March 1 of each year, the Secretary shall submit to Congress and make publicly available a report that:

(1) States, for the preceding year, separately for livestock and poultry and separately by enforcement area category (financial, trade practice, or competitive acts and practices), with respect to Investigations into possible violations of this Act--

> *(A) the number of investigations opened;*
>
> *(B) the number of investigations that were closed or settled without a referral to the General Counsel of the Department Agriculture;*
>
> *(C) for investigations described in subparagraph (B), the length of time from initiation of the investigation to when the investigation was closed or settled without the filing of an enforcement complaint;*
>
> *(D) the number of investigations that resulted in referral to the General Counsel of the Department of Agriculture for further action, the number of such referrals resolved without administrative enforcement action, and the number of enforcement actions filed by the General Counsel;*
>
> *(E) for referrals to the General Counsel that resulted in an administrative enforcement action being filed, the length of time from the referral to the filing of the administrative action;*
>
> *(F) for referrals to the General Counsel that resulted in an administrative enforcement action being filed, the length of time from filing to resolution of the administrative enforcement action;*

(G) the number of investigations that resulted in referral to the Department of Justice for further action, and the number of civil enforcement actions filed by the Department of Justice on behalf of the Secretary pursuant to such a referral;

(H) for referrals that resulted in a civil enforcement action being filed by the Department of Justice, the length of time from the referral to the filing of the enforcement action;

(I) for referrals that resulted in a civil enforcement action being filed by the Department of Justice, the length of time from the filing of the enforcement action to resolution; and

(J) the average civil penalty imposed in administrative or civil enforcement actions for violations of this Act, and the total amount of civil penalties imposed in all such enforcement actions; and

(2) includes any other additional information the Secretary considers important to include in the annual report.

(b) Format of Information Provided- For subparagraphs (C), (E), (F), and (H) of subsection (a)(1), the Secretary may, if appropriate due to the number of complaints for a given category, provide summary statistics (including range, maximum, minimum, mean, and average times) and graphical representations.

Through an earlier amendment to the Grain Standards and Warehouse Improvement Act of 2000 (PL 106-472, Nov. 2000), the P&S Act was amended to include the following language:

Section 415. Annual Assessment of Cattle and Hog Industries.

Not later than March 1 of each year, the Secretary shall submit to Congress and make publicly available a report that—

(1) assesses the general economic state of the cattle and hog industries;

(2) describes changing business practices in those industries; and

(3) identifies market operations or activities in those industries that appear to raise concerns under this Act. (7 U.S.C. 228d)