Agricultural Supply Management and Antitrust in the United States System of Agribusiness

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Agricultural Supply Management Programs

- **Private,** industry funded and administered **programs**
  - No government involvement
- The **organizations of agricultural producers** (cooperatives, associations, etc.) develop and implement these programs
  - Participation of agricultural producers is voluntarily
- The **scope** of possible activities **is broad**
  - **"Supply"** may refer to **agricultural output** at the **pre-production**, **production** and **post-production** (marketing) stages of the supply chain
- Markets affected: **dairy**, **potatoes**, **eggs**
- **Common features** of agricultural supply management programs
  - **Objective:** To achieve *a fair level of returns* for agricultural producers and *to stabilize prices* received by producers
  - **Design:** Some form of *production restrictions* and some form of *post-production supply management*

Legal Foundation: Capper-Volstead Act (1922)

- Joint activities of individual agricultural producers through their organizations = Joint activities of competitors = a cartel-type conduct
- **Sherman Act (1890)** Section 1 prohibits contracts, conspiracies and combinations in restraint of trade
    - Price-fixing and output control are illegal *per se* (a felony)
        - The most damaging in terms of market effects practices
            - Output reduction, price increase, deadweight loss
- **Capper-Volstead Act** is a *limited* antitrust exemption
- Section 1 defines the scope of activities exempt
    - *"Persons engaged in the production of agricultural products … may act together in associations … in collectively processing, preparing for market, handling and marketing … such products"*
- **Case law** makes interpretation on a case-by-case basis

Market Effects of Supply (Output) Control

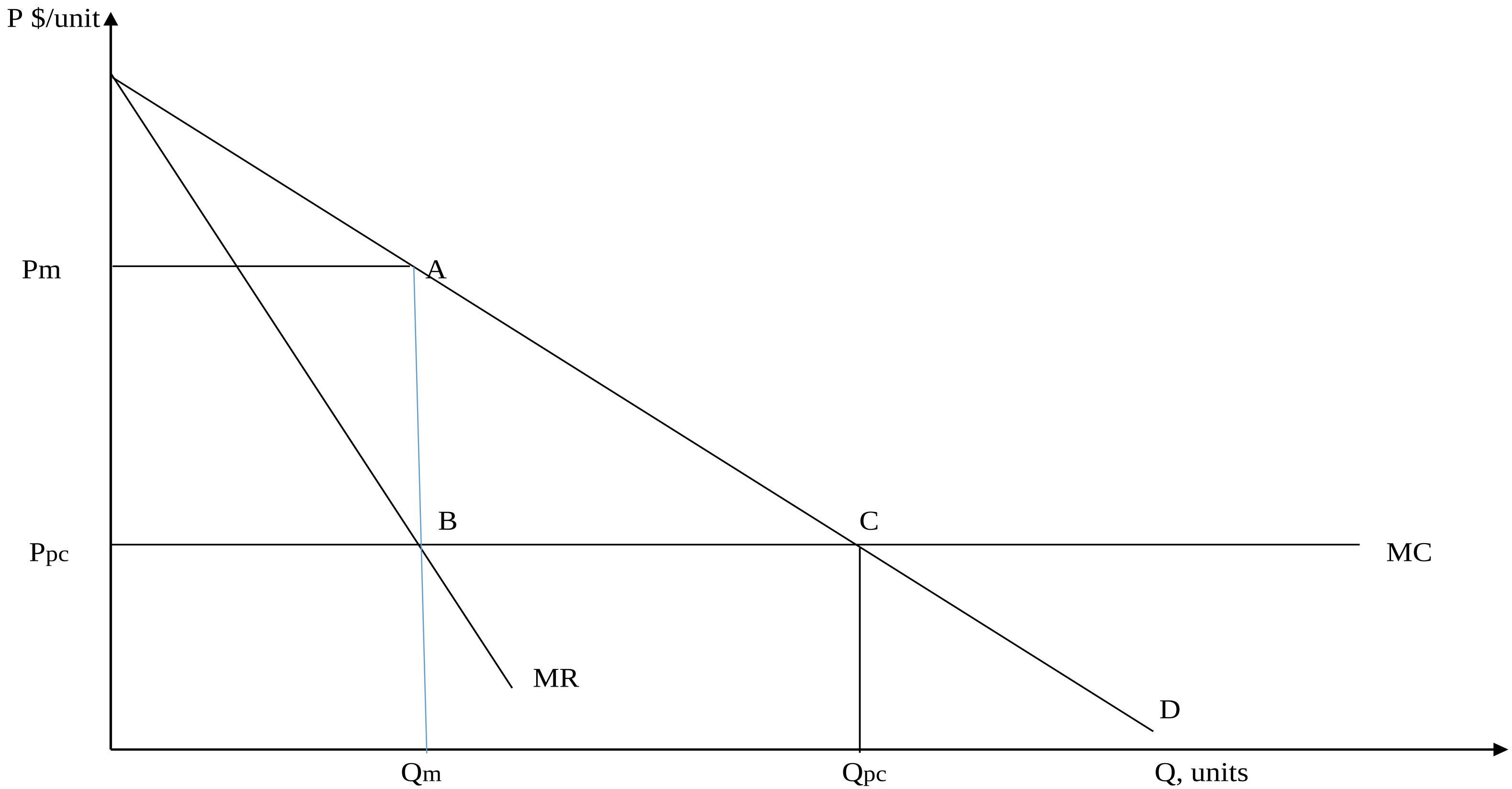

Figure 1. Perfectly Competitive (Qpc; Ppc) and Monopoly (Qm; Pm) Equilibriums.

Triangle ABC is a deadweight loss due to monopoly market power. Rectangle PpcPmAB is a monopoly overcharge. Trapezoid PpcPmAC is a reduction in the consumer surplus due to monopoly power.

Supply Management in Dairy and Potato Industries

- **Economic forces** leading to the decision on supply management
  - Over-supply of milk and potatoes, increasing output price volatility and increasing level and volatility of agricultural input prices
  - Decreasing government support and increasing exposure to international markets
  - Financial stress and adverse effects on the profitability of farmers
- **Dairy:** Cooperatives Working Together (2003-2010)
  - *Herd retirement program* was used to remove from production the entire milking herds of selected dairy farmers
  - *Dairy export assistance program* provided subsidies on export of butter and cheese
- **Potatoes:** United Potato Growers of America, United Fresh Potato Growers of Idaho and other regional cooperatives (2005-2010)
  - *Potato acreage management program* was used to control the number of potato acres planted
  - *Marketing programs* included potato flow control, exchange of marketing information and secondary marketing strategies diverting excess supply of already produced potatoes

Market Effects of Supply Management Programs

- There is **evidence** on milk and potato **supply reduction**
- Key Question: Was the supply reduction reflected in **a higher price?**
- According to empirical findings reported in the literature
- **The milk price increase ranges** (vary with demand elasticity)
  - Parkinson (2008): $0.28/cwt to $0.51/cwt
  - Brown (2009): $0.22/cwt to $1.54/cwt
  - McCay (2011): $0.21/cwt to $0.62/cwt
  - “Reference” price: $13.67/cwt
- **The potato price increase ranges**
  - Bolotova et al (2008): $2.41/cwt - $2.74/cwt
  - Bolotova (2008): $0.61/cwt
  - “Reference” prices: $3.89/cwt; $4.93/cwt; $7.78/cwt
- Results to be interpreted with caution
  - Different methodologies, data sources, data frequency, analyzed time periods and regions, empirical procedures, model specifications
  - Whether the *production cost increases* were taken into account
  - Relative to which *reference price* the price increase was calculated

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Antitrust Issues: Current/Recent Private Lawsuits

- **Allegations:** Organizations of agricultural producers use **"supply management"** practices to **manipulate output prices**
  - Prices paid by buyers/consumers increase
- **Direct buyers** sue under federal law (Clayton Act 1914)
  - Wholesalers and processors buying from agricultural producers can detect price increases immediately
  - Recover **treble damages** (i.e. three times the overcharge) +reasonable attorneys' fees
  - Incentives to sue are significant
- **Indirect buyers** sue under state antitrust and consumer protection laws

- **ISSUE:** The **case law is unclear** about **which** exactly agricultural **supply management practices are protected** by Capper-Volstead Act
  - A wide range of industry-specific practices that fit "supply management"
  - The most effective practice, **production restrictions**, is the **most controversial** today

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Antitrust Issues Raised

- A common perception among industry participants is that Capper-Volstead Act protects supply management activities, including production restrictions
  - In light of **economic theory**, the market effect of **output control is similar to price-fixing**, **which is immune** based on case law
  - A number of industries openly implemented supply management programs for several years
  - Alternative: Marketing Orders/Agreements would require federal government participation -> much more complex process and issues with WTO domestic support limits
- **In Re: Fresh and Process Potatoes Antitrust Litigation** (12-2011)
  - The **first** in Capper-Volstead Act history **interpretation of legal status of supply management practices**
  - Court "Advisory Opinion": ***"Acreage reductions, production restrictions, and collusive crop planning are not activities protected by the Capper-Volstead Act"***
- The antitrust enforcement agencies, Department of Justice and Federal Trade Commission, rely on case law in their antitrust enforcement efforts

Antitrust Issues: Legal Uncertainty

- There is a considerable degree of uncertainty surrounding legal status of various supply management practices

Concerns of antitrust authorities

- The market effects of collective actions of agricultural producers
    - Higher prices for buyers and final consumers, quantity reduction, and deadweight loss
- Agricultural cooperatives are compared to classic cartels (typically operate in oligopolistic markets = "a few" market players)
    - Presumption: they have large market shares and therefore possess market power, which allows to use output control to increase price

Response

- Ag markets - perfectly competitive environment ("many" ag producers)
- A large membership of agricultural cooperatives and uncertainty of agricultural production make agricultural output control more difficult to implement

  -> it is more challenging to achieve a sustainable price increase
- Over-supply problem: Output prices are below production costs

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Implications for Industry and Policy Decision-Makers

- *Agricultural supply management* is a measure that *effectively allows to deal with a number of economic forces adversely affecting modern agricultural production*
  - Increasing input and output price volatility, over-supply problem, low return level, middlemen market power
- Should be aware of **legal challenges**
  - During legal proceedings, supply management practices are interpreted on a case-by-case basis
    - What is "legal" for one industry may be "illegal" for another one
  - It is important to distinguish between pre-production, production and post-production supply management
    - The latter is more likely to be interpreted as "marketing activities" protected by Capper-Volstead Act
- Should be thinking about **alternative practices/programs**
  - Various forms of price control
    - "Price-fixing" has been interpreted as an element of "marketing activities" generally protected by Capper-Volstead Act
  - "Public" programs – involve government participation

Questions ???

Comments …

Thank You

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