

2008 Annual Report

Packers & Stockyards Program

United States Department of Agriculture

Grain Inspection, Packers and Stockyards Administration



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MISSION:

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

March 1, 2009

The mention of firm names or trade products does not imply that they are endorsed or recommended directly or indirectly by the United States Department of Agriculture over other firms or similar products.

2008 REPORT HIGHLIGHTS

- ❖ Packers and Stockyards Program (P&SP) *Agents achieved record levels of restitution to livestock sellers* who were unpaid from financial failures at livestock markets and with dealers (see pages 22-23).

- ❖ *P&SP's performance and efficiency measures show strong improvement.* Industry compliance with the Packers and Stockyards Act of 1921 (P&S Act) increased from 73 percent in 2007 to 80 percent in 2008, and efficiency, as measured by the decline in average number of days comprising an investigation, dropped to 77 days in 2008 from an average of 165 days in 2006 (see pages 25-27).

- ❖ *P&SP collected statistics on investigations specified by Congress* in the 2008 Farm Bill—the Food, Conservation, and Energy Act of 2008 (see page 30).

- ❖ For the second consecutive year, Packers and Stockyards Program *Agents received the USDA Secretary's Honor Award for supporting the President's Management Agenda.* This year's award was presented to the Change Agent Team for leading the design and implementation of streamlined standardized business processes (see page 32).

- ❖ A new 3-staff unit is being formed to *centralize the receipt and handling of all annual reports* submitted to P&SP for monitoring compliance with solvency, bond, livestock scales, and procurement regulations in the Western Regional Office located in Aurora, Colorado (see page 36).

- ❖ P&SP completed the 2008 *Assessment of the Livestock and Poultry Industries* as required in Section 415 of the P&S Act (see page 41).

EXECUTIVE SUMMARY

Overview—The Packers and Stockyards Program (P&SP) operates under the authority of the Packers and Stockyards Act of 1921 (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 an administrative Program Support Unit, a Business Practice Unit, a Financial Unit, and two Resident Agent Units. P&SP agents in the last four units enforce the Act through regulatory actions and investigations.

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, including weighing verification (“checkweighs”) and custodial audit reviews, determine if a regulated entity is complying with the P&S Act. In 2008, P&SP conducted 456 weighing verifications that found 38 violations; 176 custodial account audits resulted in account corrections worth slightly more than \$5 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 yearly Strategic Business Plan. The 2007-2009 Plan identifies four strategic business goals that articulate longer-term strategies into annual operational objectives. These goals are:

1. Increase the level of compliance 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 in any given year. Compliance in 2007 was estimated at 73 percent

and increased to 80 percent in 2008. In 2008, goal (3) included the development of new competition monitoring programs and new regulations in the areas of production and poultry contracts, expanding existing rules 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 the responsibility for the investigation is assumed by the USDA Office of the General Counsel (OGC). Investigation efficiency has steadily improved—investigations remained in P&SP 77 days in 2008 compared to 165 days in 2006. P&SP closed 1,267 investigations in 2008.

Initiatives—P&SP is carrying out three major initiatives that span multiple years to achieve greater industry compliance with the P&S Act and to increase our efficiency in achieving compliance. These initiatives include developing and implementing standardized business processes for key activities; modernizing management information systems to provide a single program data warehouse and automated work flow systems to capture real-time agency data; and centralizing processing of industry annual reports into a single unit in the Western Regional Office.

Accomplishments—Major accomplishments for 2008 include developing the workflow process for the central report unit and revising the annual report forms submitted by regulated entities. P&SP developed and executed 12 standardized business processes, with 18 sub-process workflows and supporting documentation that have been programmed into the first phase of the modernized information system. The automated system, which was field tested in December 2008, is comprised of a national database and the first component of an Enterprise Content Management system.

Industry Assessment—An annual assessment of the industries regulated under the P&S Act from data taken out of annual reports filed by regulated firms indicates that the four largest firms' share of the total value of livestock purchases (i.e., aggregate industry concentration) has trended down over the past 4 years. Patterns of concentration in the purchase of different types of livestock, however, have exhibited different trends. Four-firm concentration in steer and heifer slaughter and in boxed-beef production has been relatively stable in recent years, although boxed-beef concentration declined in 2007.

Concentration in poultry slaughter has trended upward since 2000. Cow and bull slaughter concentration increased between 1997 and 2007. Concentration in hog slaughter increased sharply in 2003, but has been stable since then except for a decline in 2006 followed by a return to the previous level in 2007. Concentration in sheep slaughter declined from 1998 through 2004, but has since increased slightly above the 1998 level.

Trends in the marketing practices of packers vary by species. The volume of carcass-basis purchases of cattle trended upward from 1998 through 2002, remained constant in 2003, fell in 2004, and then increased in 2007. By comparison, carcass-basis purchases of hogs generally increased from 1997 through 2007.

Historically, as carcass-based procurement has increased in volume, packers have increased the development and testing of carcass evaluation devices in the beef industry. Changes to carcass merit programs for hogs were not significant in 2007, perhaps reflecting the fact that carcass-basis purchases of hogs have stabilized at high levels in recent years as packers seem to be satisfied with the current degree of leanness in hogs.

The use of committed procurement methods by the largest beef packers increased in 2006 and 2007, but packer feeding and use of marketing agreements continue at about the same levels as the beginning of this decade. Forward contracts and packer feeding each continue to represent relatively small portions of total cattle procurement. These trends tend to be anchored to existing technologies rather than prevailing economic conditions.

If the tight credit and weak demand at the end of 2008 persist into 2009, industry contraction is almost certain to lead to greater concentration rates. These rates likely would be above those seen in the past due to consolidation that resulted from the adoption of cost-saving technologies. Greater consolidation due to overall economic contraction likely would affect the balance of power among competing businesses; market access for livestock sellers; and prices paid by consumers, producers, and processors. Such a contraction also would unfold in unpredictable ways, for example, contraction may affect one species more than another depending on consumer demand or it may affect one region more than another by altering relative-cost-of-production patterns. Regardless, indications are that 2009 will be a period of financial stress for those with interests in the livestock-meat sector, creating an unprecedented demand on the financial protections provided to livestock sellers and poultry growers under the P&S Act.

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OVERVIEW OF THE PACKERS AND STOCKYARDS PROGRAM

This section provides a brief overview of Packers and Stockyards Program (P&SP) authority and responsibilities under the Packers and Stockyards Act of 1921 (P&S Act). An overview is also provided of P&SP's position within the organizational structure of the U.S. Department of Agriculture 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, meat carcasses, 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 ends of the market channel are not under the jurisdiction of P&SP.

The P&S Act prohibits unfair, deceptive, unjustly discriminatory, and fraudulent 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 U.S. Department of Justice (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 GIPSA 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 Packers and Stockyards Program, the GIPSA Administrator is responsible for the Federal Grain Inspection Service. Within the U.S. Department of Agriculture, the GIPSA Administrator reports to the Under Secretary of Marketing and Regulatory Programs (Figure 1).

P&SP’s appropriated budget for 2008 was \$20.9 million. Applying the Consumer Price Index to actual appropriations indicates that the inflation adjusted appropriation has remained roughly constant since 2004 (Table 1).

Table 1. P&SP Appropriated Budget, Consumer Price Index, and Inflation Adjusted Funding for Fiscal Years 2004-2008

Year	2004	2005	2006	2007	2008
Actual Funds (\$K)	18,951	19,510	20,257	20,172	20,901
CPI	188.9	195.3	201.6	207.3	215.3
Adjusted Funds(\$K)	21,600	21,508	21,634	20,951	20,901

Note: Base is set at fiscal year 2008.

The Deputy Administrator of the Packers and Stockyards Program provides strategic leadership to five program directors, two in headquarters in Washington D.C. and three in regional offices in Atlanta, Georgia; Aurora, Colorado; and Des Moines, Iowa (Figure 2). P&SP employs approximately 160 staff.

Each regional director manages an administrative Program Support Unit and four program units: a Business Practice 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 five to seven 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.

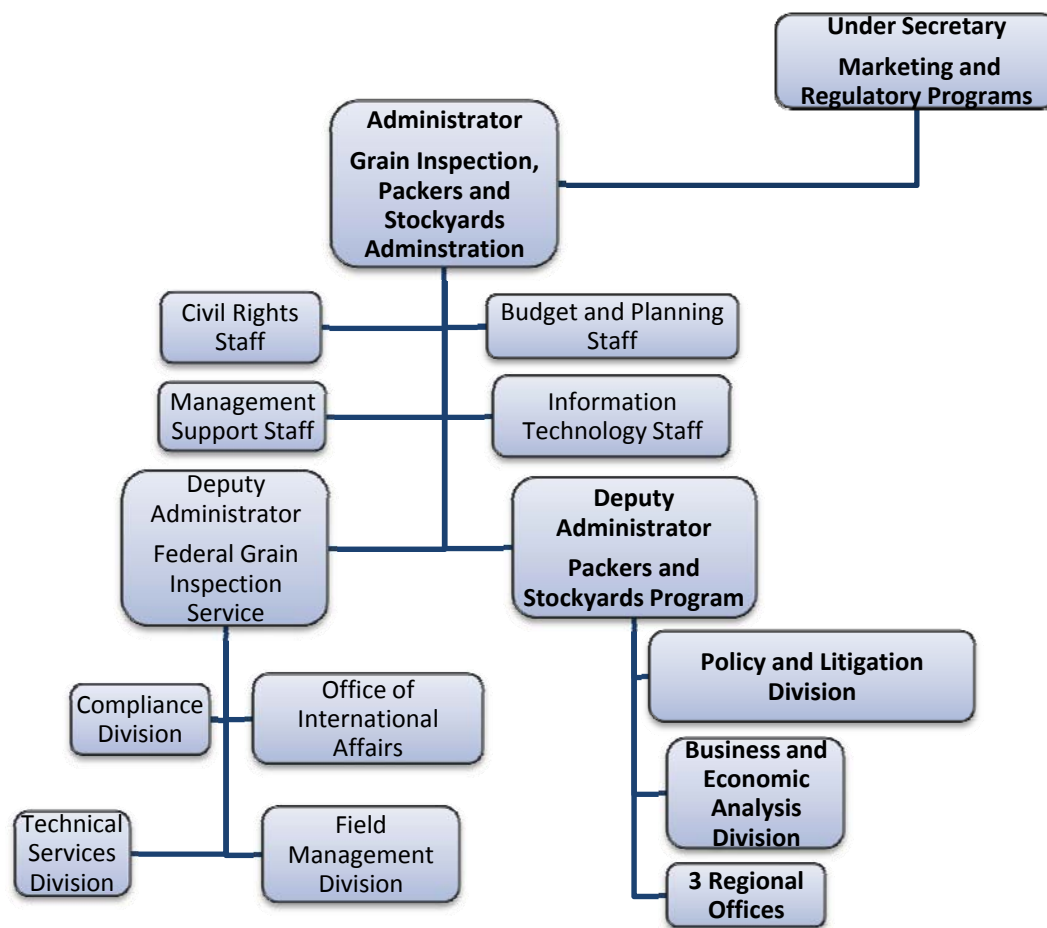


Figure 1. Grain Inspection, Packers and Stockyards Administration Organizational Structure

Each regional office is expert in one or more species of livestock. The Eastern Regional Office focuses on poultry, the Midwestern Office on hogs, and the Western Regional Office on cattle and sheep. Thirty-seven 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).

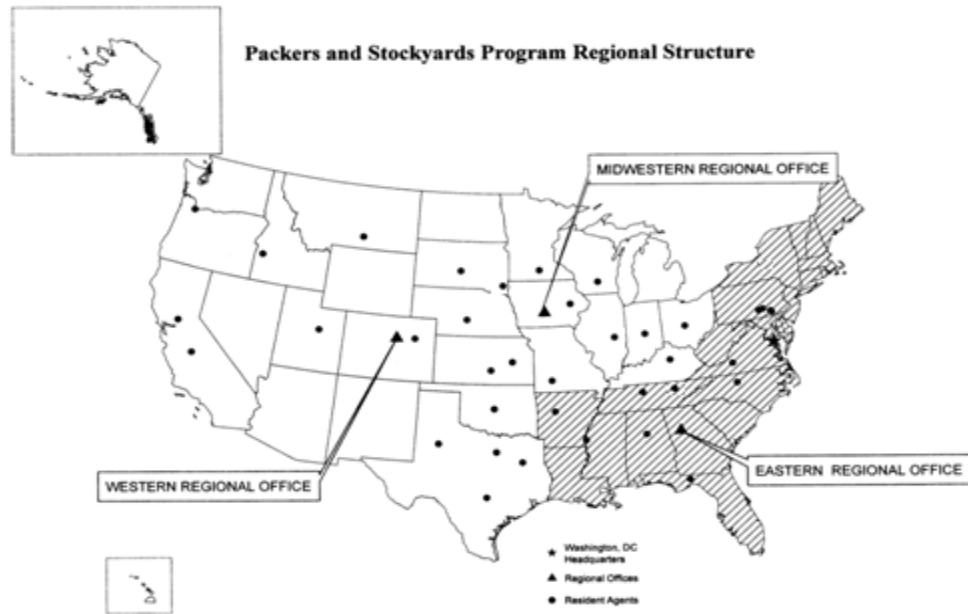


Figure 2. Packers and Stockyards Program Regional Office and Resident Agent Locations



Figure 3. Location of Livestock Packers 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 Subject to the P&S Act.

PACKERS AND STOCKYARDS PROGRAM UNIT-LEVEL ACTIVITIES

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 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 complex financial requirements of the Act. Less complex activities are conducted by resident agents who maintain close contact 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 Act, or may be initiated in response to industry-driven complaints, 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. The Agency 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; helping producers file 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, 2000-2008

Fiscal Year	Regulatory Activity	Investigation Expenses		
		Competition	Trade Practices	Financial
(Thousand dollars)				
2000	N/A	2,986	3,583	4,628
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

Table notes: “N/A” indicates data not available. Prior to fiscal year 2006, regulatory activities and investigations were not differentiated. Values for 2008 based on hours per category.

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 for admitted violations (stipulations started in 2007), or pursues litigation through USDA’s Office of the General Counsel before a USDA Administrative Law Judge or through the U.S. Department of Justice (DOJ). Litigation may result in a fine against the offending entity (Table 3), or in suspension of the entity’s P&S registration.

Table 3. Penalties Levied for P&S Act Violations, 2005-2008

Type Judgment	2005	2006	2007	2008
Stipulations	NA	NA	9,750	23,275
Administrative Penalties(\$)	114,300	196,350	404,150	657,770
DOJ Civil Penalties	NA	NA	36,500	51,240

Note: Prior to 2007, administrative and DOJ penalties were combined. In 2007, 15 Stipulations averaged \$1,552 each, 37 Administrative Penalties averaged \$17,778, and 6 DOJ Civil Penalties averaged \$8,540.

Activities Enforcing Business Practice Provisions

In 2006, the P&SP merged its regional offices' Trade Practices and Competition Units to consolidate their functions under a single supervisor and more closely reflect that trade practice and competition violations form a continuum in the market. For example, prices have a central role in guiding and directing the economy in a truly competitive market. Prices provide signals that guide producers' decisions about when and where to market. Producers cannot effectively respond to such signals if prices inaccurately reflect costs or cannot be compared during the bargaining process. A trade practice violation, such as inaccurate weighing that incorrectly values hundreds, if not thousands, of carcasses, thus not only defrauds the producer but also creates a price distortion that interferes with truly competitive market decisions.

The business practices units, supported by resident agents, conduct investigations of alleged anti-competitive practices and unfair and deceptive trade practices at auction markets, 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.

As noted, trade practice violations can evolve into competition violations when they affect significant numbers of buyers, sellers, or both. This underscores how the nature of the illegal behavior is relevant when considering plans for investigation and litigation. Similar consideration must be given in distinguishing anti-competitive practices along another classification line: exploitive versus exclusionary behavior. Exploitive behavior includes a firm using monopsony power to lower the procurement price of livestock purchased from sellers. The misuse of the market power causes direct and immediate harm to the seller. Exclusionary anti-competitive behavior denies an individual or a group access to a market. For example, a non-business-based decision to refuse to deal with a given individual or entity is an example of exclusionary behavior. Exclusionary anti-competitive behavior and trade practices that may develop into anti-competitive behavior emphasize the need for P&SP investigators and legal specialists to work closely with OGC in planning investigative work.

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 OGC on all competition investigations. When the results of the investigation indicate that the evidence and circumstances support legal action, P&SP then formally refers the case file to OGC for action.

P&SP conducts many activities that monitor changes in industry structure 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 three next sections.

Fed Cattle Price Monitoring

P&SP undertook an initiative to respond to market issues that evolved from the announcement of the first case of Bovine Spongiform Encephalitis (BSE) in the U.S. 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 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 statistical model is similar to the model used by the Federal Trade Commission in 2008 to monitor retail gasoline prices.

The current 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 19 regulatory activities in 2008, and of these, 4 indicated cause for investigation (Table 4).

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

Fiscal Year	Regulatory Activities Initiated	Investigations Initiated
2006	25	6
2007	13	0
2008	19	4

Of the four investigations initiated in 2008, three were completed and one is ongoing. None of the completed investigations discovered any competition violations. Although no competition violations have been identified, with the ongoing program P&SP actively monitors market prices on a weekly basis and initiates timely regulatory reviews and investigations, if necessary, of observed market price anomalies.

Cow and Bull Monitoring Program

This proactive monitoring program was conducted by P&SP during 2005-2008 to monitor the Nation's cow and bull packers. Specifically, procurement and sales patterns were reviewed to identify potential violations of the Act and accumulate information that could be useful for subsequent investigations. P&SP reviewed

15 packers that slaughtered more than 100,000 cows and bulls annually. These packers slaughter more than 80 percent of the federally inspected cows and bulls each year and make most of their purchases at livestock auctions. By investigating cow and bull packers and aggregating and analyzing information that investigators currently collect during other types of investigations at livestock auctions, P&SP was able to (1) define the cow and bull markets, and (2) monitor the cow and bull markets for violations of the P&S Act. When P&SP found evidence of a specific violation through the monitoring program, a detailed investigative workplan was developed and executed.

The Cow and Bull Monitoring Program resulted in the discovery of two potential competition violations that P&SP investigated. The first was the investigation of a packer for a potential violation of Section 201.67 of the regulations, which prohibits packers from owning an interest in, financing, or participating in the management of a market agency selling on commission. The investigation resulted in a complaint being filed against the packer under an on-going investigation.

The second was the investigation of the cow and bull market in the Southeastern United States. The investigation found a group of packers that apparently failed to conduct their buying operations independently of and in competition with each other as required under regulation 201.70. In 2008, P&SP issued Notices of Violation to the involved packers informing them of P&SP's findings. In 2009, P&SP will follow up to ensure that the packers have brought their operations into compliance with the P&S Act and regulations.

The monitoring program also met its goal of obtaining data and other information for use in subsequent competition investigations in the market for slaughter cows and bulls. For example, in 2005, P&SP relied on the data obtained from the Cow and Bull Market Monitoring Program to investigate the estimated impacts of a merger among cow and bull slaughterers. The investigation accurately identified a number of auction markets that could be adversely impacted by the merger. P&SP is monitoring those markets to guard against anti-competitive activity.

Committed Procurement Review and Audit

P&SP monitors the use of “committed procurement” arrangements, which commit cattle to a packer more than 14 days prior to delivery. Each year, P&SP economists obtain fed cattle procurement data for the previous calendar year from the five largest beef packers. If the packers change their procurement arrangements with suppliers from previous years, P&SP also collects any new or modified written fed cattle 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 for fed cattle. Finally, P&SP economists reconcile the calculations based on the detailed transaction data with committed procurement reported on the Packer Annual Reports of the five largest packers.

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. In 2008, P&SP met with two of the major beef packing companies. These meetings resulted in a clear, mutual understanding of the reporting of fed cattle committed procurement and more reliable reporting and calculation of the packers’ reliance on committed procurement methods.

Packer Contract/Marketing Agreement/Procurement Monitoring

Relying on written contracts and other information collected during the Committed Procurement Reviews, P&SP investigators analyze the various procurement and pricing methods used by steer and heifer packers. P&SP investigators obtain and review all available contracts and agreements 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.

Other Competition Activities in 2008

The P&SP Competition program also continuously analyzes significant industry events and industry mergers and acquisitions. Though P&SP does not have statutory authority to block mergers

or acquisitions, P&SP provides merger and acquisition analyses to the DOJ and Federal Trade Commission (FTC) for their evaluation of mergers and acquisitions. The merger analyses are also used within P&SP to assess the mergers' estimated impacts.

In 2008, P&SP conducted an analysis of the proposed JBS Swift and Company acquisition of National Beef Packing, LLC, and Smithfield Beef Group, Inc. P&SP provided that analysis and other advisory assistance to the DOJ for its evaluation of the proposed acquisition.

On August 26-27, 2008, P&SP held a meeting in Washington, D.C., for economists and legal specialists assigned to the Business Practices Units. The meeting included presentations from the FTC on their consumer protection work. Another session at DOJ's Antitrust Division reviewed DOJ merger analysis procedures and how P&SP's analyses are used, so that P&SP could enhance its understanding of the process in order to better contribute.

P&SP and OGC also collaborated in 2008 with the Commodity Futures Trading Commission (CFTC) by providing information and analysis of livestock and meat marketing issues that are jointly relevant to P&SP and the CFTC's regulatory and enforcement activities.

Currently P&SP is working with USDA's Economic Research Service to develop a generally applicable form of competition monitoring based on cost-price ratios. The approach could be applied, for example, to monitor the average price of a poultry contract reported by a particular firm compared to a statistical average that represents its estimated payment. Large variances between the observed and predicted costs would serve as the trigger for a field audit to explain the variance, recognizing at the outset that many factors could legitimately explain the variance.

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 after market operations begin 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 orientation for feed mill operators 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 conducts procurement compliance reviews of subject firms to determine if unfair or deceptive trade practices are occurring in the procurement of livestock, meat, and poultry in violation of the P&S Act. 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. Inspections and Violations Found, 2005-2008, for Scale and Carcass Checkweigh Evaluation Instruments.

Type of Checkweigh	2005	2006	2007	2008
<i>Inspections</i>				
Auction	161	89	137	188
Dealers	22	11	21	14
Packers	17	6	14	13
Carcass Checkweigh	2	4	106	82
Poultry Checkweigh	53	100	87	58
Tare Weight Rpt	21	8	93	50
MPI Surveillance	2	1	0	0
Feed Checkweigh	28	51	76	43
Carcass Evaluation	16	12	10	8
Total Inspections	322	282	544	456
<i>Violations</i>				
Auction	13	4	8	14
Dealers	0	0	0	1
Packers	1	0	0	0
Carcass Checkweigh	0	0	10	4
Poultry Checkweigh	9	5	4	4
Tare Weight Rpt	0	1	37	8
MPI Surveillance	0	0	0	0
Feed Checkweigh	2	6	5	5
Carcass Evaluation	3	2	1	2
Total Violations	28	18	52	38

Any apparent change in purchase weight that is caused by a person, such as modifying the actual weight of the livestock or failing 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.

Activity 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 to investigate the problem.

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 commonly called a "custodial account" to hold proceeds from the sale of consigned livestock. 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, P&SP acts to have the account balance corrected (Table 6).

Table 6. Number of Market Audits and Shortages Corrected Through On-site Investigations, 1998-2008

Fiscal Year	Custodial Account Audits	Markets With Shortages	Corrected by On-Site Investigation
1998	393	187	\$3,690,355
1999	233	103	\$2,701,091
2000	374	154	\$5,916,746
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

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, 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 poultry or poultry products.

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 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. A seller who does not receive payment on a transaction must file a bond claim within 60 days of the transaction in order to be eligible to receive payment under the bond. 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 bond surety or trustee as a courtesy to the industry. 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. A large packer failed in 2002, owing more than \$15 million to producers.

Since 1998, 11 dealers on average have failed per year, ranging from 31 to 1 in a single year. Percent restitution to livestock sellers from all sources has averaged 20 percent per year, with a high of 55 percent and a low of 5 percent (Table 7).

Table 7. Total Dealer Financial Failures and Restitution, 1998-2008

Fiscal Year	No.	Owed for Livestock (\$)	Restitution From Bonds (\$)	Restitution From Other Sources (\$)	Percent
1998	10	685,726	133,345	61,435	28
1999	10	1,684,128	291,261	38,024	20
2000	11	1,464,733	324,979	91,800	28
2001	11	2,841,305	317,444	24,786	12
2002	11	3,271,962	618,764	60,000	21
2003	5	1,805,600	112,281	28,923	8
2004	3	770,860	95,000	0	12
2005	1	2,993,990	0	0	0
2006	13	3,018,131	134,936	26,856	5
2007	31	6,941,930	257,634	549,303	12
2008	20	2,054,647	843,682	301,916	55

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. A large dealer failed in 2005, owing more than \$1 million in unprotected livestock debt. Since 1998, an average of 5 auction markets has failed per year, ranging from 11 to 2 in a single year. Consignors received average restitution of 52 percent, with actual restitution ranging between 98 and 29 percent (Table 8).

Table 8. Total Auction Market Financial Failures and Restitution, 1998-2008

Fiscal Year	No.	Owed Consignors (\$)	Restitution From Bonds (\$)	Restitution From Other Sources (\$)	Percent
1998	2	225,001	66,131	0	29
1999	3	862,666	60,000	424,589	56
2000	4	399,023	100,193	186,113	71
2001	4	1,104,985	133,745	519,265	59
2002	6	1,082,034	378,610	0	35
2003	6	1,187,979	211,464	138,848	30
2004	2	145,772	60,000	16,649	53
2005	3	336,006	85,000	201,840	78
2006	9	979,543	267,174	19,380	29
2007	11	511,704	37,252	155,890	38
2008	6	602,100	237,734	352,111	98

Bond payout for packers from 1998 to 2006 ranged between a low of 0 to a high of 93 percent with an average of 20 percent (Table 9). Packer bond payout rates ranged between 0 and 93 percent over the 11 years. On average, in any one year 3 packers will suffer financial failures owing livestock sellers \$2,977,956 with a bond payout of \$494,316, or 20 percent of the valid claims.

Table 9. Total Packer Financial Failures and Bond Payout, 1998-2008

Fiscal Year	No.	Owed for Livestock (\$)	Payout from Bonds (\$)	Percent
1998	4	71,756	66,657	93
1999	4	611,067	30,000	5
2000	3	686,924	25,000	4
2001	1	81,735	50,000	61
2002	3	18,158,330	4,939,977	27
2003	3	2,600,469	88,235	3
2004	1	927,654	162,336	17
2005	2	1,232,477	20,000	2
2006	5	1,899,712	35,267	2
2007	6	4,057,002	20,000	0.5
2008	4	2,430,394	0	0

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. Presently, P&SP is evaluating a risk-assessment model that combines statistical methods, accounting theory, and the operating history of entities as a tool to gauge the potential for behavior that may violate the Act, such as operating while insolvent.

PACKERS AND STOCKYARDS PROGRAM MANAGEMENT

The Packers and Stockyards Program executes its management function through tactical annual goals and strategic multi-year goals. The primary method for monitoring and communicating these goals to all employees is a yearly Strategic Business Plan. The 2007-2009 Plan identifies four 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.

The next section addresses the methods P&SP uses to improve performance and efficiency, and the results P&SP is demonstrating in achieving these goals.

The section following that then presents management initiatives that span multi-year horizons and support achieving higher performance and efficiency. The initiatives include the development of a 3-staff unit to process annual reports filed by businesses regulated by P&SP, the ongoing business process re-engineering, and the development of a single, comprehensive P&SP database integrated with the workflow processes constructed in the business process re-engineering.

P&SP has three smaller, though extremely important, management initiatives. The first is a training initiative. During 2007, all personnel with investigative and regulatory responsibilities (roughly 95 percent of the workforce) participated in formal training at the Federal Law Enforcement Training Center in Glynco, Georgia. New personnel are being sent to the Center when the number of new staff reaches a class size. P&SP is also pursuing legislative initiatives and new regulations (see *Industry Concerns* section). Finally, P&SP is revising its Employee Manual to provide a Web-accessible guide that complements the new standardized operating procedures.

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 all activities P&SP conducts that directly or indirectly influence industry compliance. P&SP calculates industry compliance based on random samples similar to manufacturing quality control programs. In 2008, industry compliance was 80 percent, up from 73 percent in 2007.

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 the case is forwarded to headquarters) of investigations. Results show the time has declined from 165 days in 2006 to 77 days in 2008. The time to conduct the investigative phase is only one measurement in the complex process of conducting an investigation. Additional information about efficiency measures appears below.

Performance

P&SP's overall performance rate is a composite index of five program-wide audit and inspection activities: 1) solvency audits of firms identified as being at high risk of failure (i.e. by a statistical model based on financial ratios that the regulated entities report annually), 2) financial audits of a random sample of a firm's custodial accounts with the sample size set to yield 90-percent confidence when inferred to the population of regulated entities; 3) financial audits of the prompt pay records of a random sample of firms with sample size set to yield 90-percent confidence; 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, designed to yield population estimates at a 90-percent confidence level. The aggregated industry compliance rate index reflects the statutory and regulatory compliance of the regulated industry with the P&S Act (Figure 7).

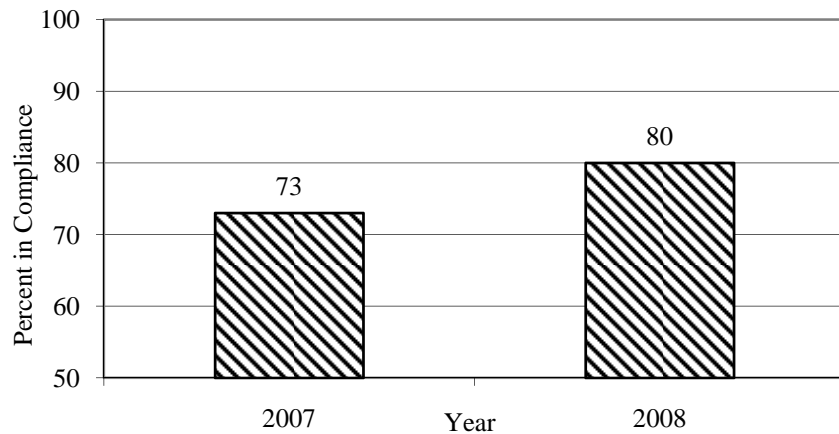


Figure 7. Aggregated Industry Compliance From Random Samples, 2007 and 2008

Financial audits are carried out in accordance with general accounting standards and supervised by staff with certified public accounting status. Business practice inspections 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 that were designed in conjunction with a private consultant in adherence to P&SP Standard Operating Procedures Manual (June 2007).

Audit and inspection results show an increase in compliance rates in 2008 for three out of the five areas reviewed and no change in a fourth, with livestock dealer and market scales the sole category that declined. Data available for 2 years show that compliance with each component tends to be similar, although compliance is highest with packing scales and solvency requirements (risk audits) and lower for prompt pay and custodial account maintenance (Figure 8).

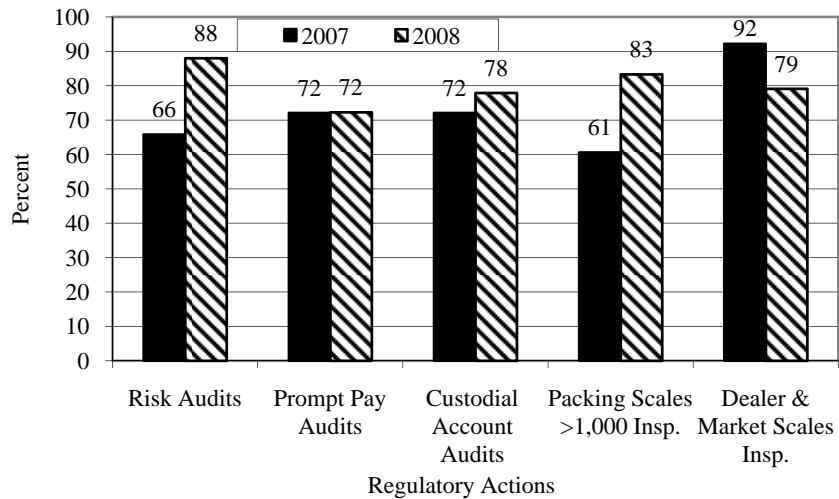


Figure 8. Comparison of 2007 and 2008 Performance Measure Components

Efficiency

P&SP measures its efficiency using the metric of the time between initiating an investigation and its closing in P&SP or until the investigation is referred to the USDA Office of the General Counsel. After this point P&SP and OGC usually work together reviewing the case to determine evidence and witness availability and weight and on preparation of the case for filing. The measure describes the time required by P&SP to complete the investigation prior to seeking involvement by OGC. P&SP has reduced the number of days in the investigative phase of investigations dramatically over the past 3 years. In 2006, the average was 165 days; in 2008 it decreased to an average of 77 days (Figure 9).

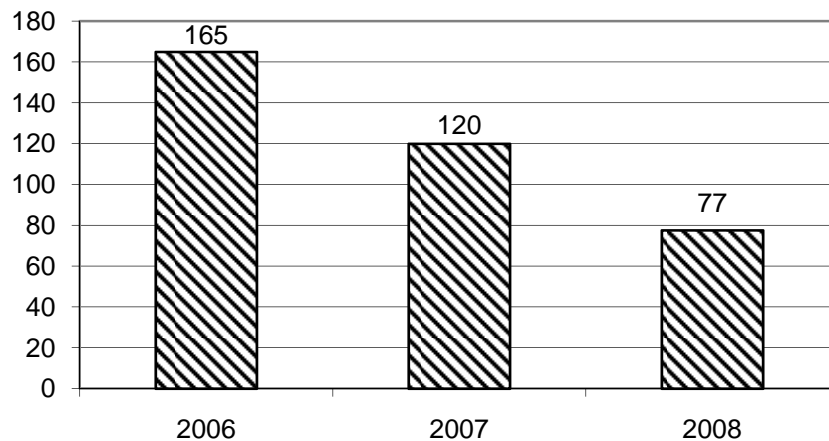


Figure 9. Days in Investigation From Opening to Referral to OGC, Investigations Closed in FY 2008

The decrease in 2008 occurred despite a sharp increase in the total number of investigations and regulatory activities (Table 10). The data in Table 10, in contrast to Figure 9, are total days to closure, averaged across cases closed by P&SP without referral to OGC and those cases closed after referral to OGC.

Table 10. Number of Investigations and Regulatory Activities Closed During Fiscal Year, and Activities Open at End of the Fiscal Year, by Location of Activity, 2008 vs. 2007

Type and Location	Number		Percent Change	Average Days		Percent Change
	2007	2008		2007	2008	
<i>Investigations Closed</i>						
Field	354	370	4.5	120	209	74.2
Office	381	897	135.4	84	101	20.2
<i>Investigations Open</i>						
Field	198	228	15.2	277	362	30.7
Office	138	220	59.4	100	263	163.0
<i>Regulatory Activity Closed</i>						
Field	893	1180	32.1	38	35	-7.9
Office	299	84	-71.9	129	91	-29.5
<i>Regulatory Activity Open</i>						
Field	55	30	-45.5	155	103	-33.5
Office	22	18	-18.2	267	128	-52.1

Table note: “Field” activities are conducted at regulated business entity locations. “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: competition, trade practice, or financial violations.

Competition violations may involve contract arrangements and procurement, some payment practices, and preferential treatment or restriction of competition through apportionment of territory. Trade practice violations include misuse of scales and 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. Financial violations include misuse of custodial accounts, failure to pay or remit, slow pay, and tariff misrepresentation (Table 11).

Table 11. Number of Closed Investigations, 2008, by Investigative Category and Type

Category and Type	Number
<i>Competition</i>	
Restriction of Competition	8
Preferential Treatment	5
Concentration/Industry Structure	1
Other	1
<i>Financial</i>	
Delinquent Report	337
Failure To Pay or Pay When Due	141
Custodial Account	83
Solvency	58
Other	21
<i>Trade Practice</i>	
Weighing Practices and Scales	262
Bond Activities	175
Registration/Jurisdiction	76
Unfair/Deceptive Practices	50
Contract Poultry Arrangements	15
Other	13
Inadequate or False Records	10
Reparations	7
Tariff	2
Grower Termination	2
Total	1,267

P&SP's regulatory and investigative actions often find that entities are in compliance with the P&S Act. When non-compliance is alleged, P&SP either assesses fines, or stipulations, for admitted violations or pursues litigation action 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 the U.S. Department of Justice (DOJ).

In fiscal year 2008, P&SP opened 1,402 cases, of which 1,387 were alleged violations for financial or trade practice behaviors. During the fiscal year, P&SP closed 1,178 cases without referring them to OGC (Table 12). An additional 89 cases were closed after referral to OGC.

Table 12. Investigations by Type and Category, and Average Days in Stages for Closed Investigations Indicating Enforcement Action.

Status & Type	Average Days				Number
	In PSP	Referral to Filing	Filing to Resolution	Start to Resolution	
<u>A. Total Investigations Opened</u>					
<i>Livestock</i>					
Competition					15
Financial					706
Trade Practice					613
<i>Poultry</i>					
Financial					13
Trade Practice					55
Total					1,402
<u>B. Total Investigations Resolved and Closed by P&SP</u>					
<i>Livestock</i>					
Competition	232			232	14
Financial	47			47	568
Trade Practices	78			78	536
<i>Poultry</i>					
Financial	35			35	9
Trade Practices	57			57	51
Weighted Averages & Sub Total	64			64	1,178
<u>C. Total Referred to OGC and Closed</u>					
<i>Livestock</i>					
Financial w/o Admin Action	165			502	20
Financial w/ Enforcement Action	281	396	223	899	40
Trade Practice w/o Admin Action	329			945	7
Trade Practice w/Enforcement Action	303	212	199	714	16
<i>Poultry</i>					
Competition w/o Admin. Action	517			574	1
Weighted Averages & Sub Total	264	229	144	769	84
<u>D. Total Referred to DOJ Through OGC and Closed</u>					
<i>Livestock</i>					
Financial no Civil Action	111			274	3
Financial w/ Civil Action	97	152	76	500	2
Weighted Averages and SubTotal	105			473	5
Averages & Total Closed	77			747	1,267

Table Notes: “w/o Admin Action” indicates that P&SP closed the case without filing a formal administrative enforcement action after referral to OGC. These cases include files referred to OGC for referral to DOJ that were returned to P&SP without referral. The “Referral to Filing” column reflects days pending filing action by OGC or DOJ. In section C this 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. During the “Referral to Filing” period, the cases continue to be developed through interaction between OGC and P&SP. Cases that are referred may not be ready for administrative action without update, confirmation of witness testimony and availability, sufficiency of evidence, etc. 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, with 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 64 days. Another 89 cases were resolved that had been referred to OGC. Cases are referred to OGC when the investigation is determined by P&SP staff to be complete or require cooperation with OGC. Frequently in competition and cases surrounding large financial failures, OGC and P&SP continue to work on the evidence and investigation, working toward the filing of a complaint. The average number of days for cases referred to OGC is calculated based on whether the cases were referred to DOJ. Cases not referred to DOJ required on average 264 days in P&SP; cases referred to DOJ required 105 days in P&SP. Table 12 represents only cases that were closed in 2008; note some cases were referred to OGC in years prior to 2008. As a result of referrals from P&SP, OGC filed a total of 59 new administrative actions and referred 29 cases to DOJ in FY 2008.

Management Initiatives

In 2008, P&SP began or continued work on three major initiatives: 1) standardization of the program's business processes—such as conducting a custodial audit at a livestock market; 2) a new management information system; and 3) a centralized reporting unit for the receipt of reports from the industry. These initiatives, while not strictly a response to the 2006 Office of the Inspector General report on P&SP, are consistent with strengthening areas of weakness identified in that audit. P&SP initiatives, however, go substantially beyond deficiencies identified in the 2006 Office of Inspector General (OIG) report.

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. In 2006, P&SP's average score across the 17 dimensions of the survey was 45; in 2008, the score improved significantly to 66. This average score was 22 percent higher than the Government wide benchmark average, and P&SP scored higher than the benchmark median in all but 2 of the 17 individual elements of survey. The participation of staff in major management initiatives has been a significant factor in improving employee

attitudes and morale. Our employees have received recognition for their contributions at the highest levels of USDA. For two consecutive years, P&SP teams have received the USDA Secretary's Honor Award. In 2007, a team of agents was recognized for maintaining the accuracy of industry scales that weigh livestock. In 2008, a second P&SP team was recognized by the Secretary for leading P&SP's business process re-engineering initiative.

The team that led the business process re-engineering initiative, the Change Agents Team, was comprised of 14 employees from regional offices and headquarters. The team's charge was to develop standard work processes and operating procedures for P&SP's major activities. Their work also paved the way to a modern computerized management information system. As an additional outgrowth of this activity, P&SP established a Continuous Improvement Program, which solicits recommendations from all P&SP employees and acts on those that show promise for further improving program operations.

To illustrate the work being conducted in these initiatives, there are three subsections following the OIG Audit sub-section below. The first of the sub-sections to examine the management initiatives (the second sub-section below) provides an overview of the 12 major core business processes adopted and implemented during 2008, as well as 11 sub-processes in the *Investigation Process* and 7 in the *Regulatory Activity Process*. The second subsection describes the ongoing effort of P&SP to modernize the computerized management of information with the creation of PSAS, Packers and Stockyards Automated System.

The final subsection describes a new Centralized Reporting Unit (CRU) that will consist of three staff members located in the Western Regional Office in Aurora, Colorado. The CRU subsection describes the operation of the unit and efficiencies the unit will bring to P&SP. The discussion of the CRU's business process also provides an example of standardized business processes developed by the Change Agents Team.

OIG Audits

In April 2005, OIG initiated an audit of P&SP's management and oversight. OIG issued its report (*30601-01-Hy—Grain Inspection, Packers and Stockyards Administration's Management and Oversight of the Packers and Stockyards Programs*) on January 10, 2006. The report cited 4 major findings and provided 10

recommendations. P&SP concurred with the findings and recommendations, and during fiscal years 2006 and 2007 significantly improved management controls and strengthened program policy and delivery. On March 16, 2007, USDA's Office of the Chief Financial Officer (OCFO) notified P&SP that all of the planned corrective actions were completed and that no further reporting to OCFO on P&SP's response to the audit was necessary.

In early 2008, P&SP requested that OIG conduct a followup audit to obtain an independent assessment of the progress in improving the efficacy and efficiency of P&SP. OIG began conducting field and headquarters reviews in May 2008; as of December 2008, P&SP is awaiting the results of the audit.

P&S Business Process Re-engineering

In 2006, P&SP initiated a program-wide Business Process Re-engineering (BPR) effort to develop workflow process descriptions for all of its major activities. All regional offices and headquarters divisions participated. Phase 1 of the BPR process in 2006 required each regional and headquarters office to analyze its existing procedures. Next, P&SP improved the efficiency and consistency of the identified core processes throughout P&SP. The third and final phase, which is ongoing, involves implementing the 12 updated core processes. Eight primary core processes are being implemented in the regional offices and four at headquarters.

Table 13. Primary Core Business Processes Implemented by Program Office

Regional Offices

- Entity Registration and Bonding
- Regulatory Activities
- Investigations
- Enforcement (Regional Office responsibilities)
- Bond and Trust Claims
- Financial Instrument Termination/Expiration
- Scale Test Report
- Entity Annual Report Filing

Policy and Litigation Division

- Enforcement (Headquarters responsibilities)
- Policy and Regulation Promulgation

Business and Economic Analysis Division

- Economic and Statistical Analysis and Reporting
- PSAS Change Control

In the regional offices, *Entity Registration and Bonding* improves the registration process and ensures compliance with financial security requirements for entities subject to the Act. *Regulatory Activities* strengthens monitoring activities that determine if a regulated entity is complying with the Act. *Investigations* clearly defines actions to be taken by P&SP agents if there is reason to believe a violation of the Act is occurring or has occurred. *Enforcement* prescribes regional office actions when a violation has been identified. *Bond Trust Claims* defines actions to settle transactions when entities encounter financial problems or when claims are filed as a result of a disputed transaction. *Financial Instrument Termination/Expiration* spells out procedures followed for expiring letters of credit attached to trust agreements. *Scale Test Report* and *Annual Report Filing* processes improve regional offices' management of filed industry reports.

At headquarters, the *Enforcement* process is an extension of the regional enforcement process, streamlining headquarters approval of steps taken during enforcement activities. The *Regulation Promulgation* process provides a system to guide and track development of rules used to enforce the P&S Act. The *PSAS Change Control* process will manage and develop suggested additions or updates to the new automated system.

The Investigations and Regulatory Activity processes both have sub-processes, which are specific tasks within each general process type (Table 14). The Investigation process includes 11 sub-processes; 7 sub-processes comprise the Regulatory Activity processes. Each sub-process has a mapped workflow that uses spreadsheet modules as automated checklists to help agents conduct an investigation or regulatory (business compliance) review. These modules were adopted and implemented in June 2008, and are undergoing operational adequacy tests. The sub-processes are enhancing efficiency through documented business processes and ensuring the uniformity of enforcement across all regions.

Table 14. Investigation and Regulatory Workflow Process Sub-Processes

Investigation Process Sub-Processes

Annual and/or Special Report
Checkweigh
Custodial Shortage or Misuse
Failure To Have Scale Tested
Failure To Remit
Failure To Pay
Inadequate Financial Instrument
Livestock Checkweigh
Operating Without Registration
Operating Without Financial Instrument
Weight and Price

Regulatory Activity Process Sub-Processes

Checkweigh Review
Dealer Buying On Commission Review
Market Review
New Entity Orientation
Packer Review
Poultry Review
Sale Day Market Review

Management Information Systems

As a result of the Business Process Re-engineering effort, P&SP standardized business practices across the agency and then focused on automating P&SP's information management system. The automated system will strengthen P&SP's ability to track major milestones of the core processes. Previously, P&SP used three separate database systems to store critical data. An integrated system was necessary to eliminate multiple data entry and ensure accurate data for reporting and management. The Packers and Stockyards Automated System (PSAS) was developed in response to this need.

PSAS is comprised of Enterprise Content Management (ECM) and Account Management System (AMS) components. The ECM is the heart of the system, managing the workflows developed from the core processes and documents generated as part of those processes. The AMS is used to store and manage regulated entity business data, support queries, generate batch letters, and for reporting.

PSAS is being implemented in Phases (Table 15). Phases 1 and 1.2 were fully implemented in FY 2008, and Phase 2 was implemented in December 2008. Phase 2 is a major software release that includes the workflows for four core processes. With the implementation of Phase 2.2 in mid-2009, the automation of all core processes will be achieved. The estimated cost of the entire system is \$2.7 million. Upon completion, maintenance and system support is projected to cost \$300,000 annually.

Table 15. PSAS Phases, Implementation Dates, and Descriptions

<i>Phase 1.0, June 2008</i>
Implemented. Account Management System (AMS) Database for business entities, facilities, scales, financial instruments, custodial accounts, entity detailed report, and list maintenance.
<i>Phase 1.2, Sept. 2008</i>
Implemented. Fixed known errors. Added scale test, letters, & entity reports; added scale test tab to scale module; Tele-Address integration.
<i>Phase 2.0, December 2008</i>
Enterprise Content Management (ECM) Workflow Phase 1 and AMS Integration. ECM Phase 1 includes workflows for Investigations, Regional Office Enforcement, Regulatory Actions, Involuntary Registration and Bonding, and Voluntary Registration Completed
Phase 2.0 will include: Investigations Module; Regulatory Activities Module; Region Enforcement Module; Violations Module; Recoveries Module; Add Tabs to Business Entity Module; Annual Reports Module; Validation Rules; New Tabs in AMS; Non-Bonded Packers; Faxing Capability; Annual Letters/Remaining Real-Time Reports.
<i>Phase 2.1a February 2009</i>
Annual Reports Workflow with AMS Integration.
<i>Phase 2.1b April 2009</i>
ECM Policy and Litigation Division Enforcement Workflow.
<i>Phase 2.2 Summer 2009</i>
Additional AMS Enhancements and ECM Scales Workflow.
<i>Phase 3.0 Summer 2009</i>
Claims Module; PSAS Database Warehouse Capability; ECM tracking of Quality Program Improvements and Regulation and Policy development.

The Central Reporting Unit

Under the P&S Act, P&SP requires that regulated businesses submit annual and special reports. The agency seeks the information to enforce financial, trade practice, and competition provisions of the P&S Act.

P&SP receives approximately 6,500 annual reports. Currently, each of the three regional offices maintains staff to manually mail annual report reminder letters and receive reports. The regions enter some of the data in local databases, perform analyses, and

scan paper copies into electronic files. These scanned reports are then printed at headquarters, and their data are entered into a headquarters database for additional analysis and subsequent policy making. The current data entry process is labor-intensive and redundant.

P&SP is establishing a Centralized Report Processing Unit (CRU) in the Western Regional Office to consolidate annual reporting activities. The development of CRU has required three major steps: designing new industry reporting forms, developing business workflows for the new unit, and developing the integrated software to capture the report data.

As part of its efforts to increase efficiency in the collection and analysis of data for enforcement purposes, P&SP has revised the forms that are used to collect data from entities subject to its regulations. The form revisions include three general types of changes.

First, the annual report forms were redesigned to simplify the forms' layouts, clarify data entry requirements, and to collect only essential information. Second, when possible, forms were combined or discontinued to reduce the paperwork burden of regulated entities. Third, the revisions tend to align a proposed form with a type of regulated entity and eliminate mailing more than one form to an entity by combining some forms (Table 16).

Table 16. Form Titles, Proposed Number Designations, and Old Number Designations

New Nr.	Form Title	Old Nr.
3001	Annual Report of Dealer	3300
3002	Annual Report of Live Poultry Dealers	3600
3003	Annual Report of Market Agency	3400
3004	Annual Report of Packers	3000
3005	Annual Report of Packers Supplement for Plants	3100
7001	Special Report Status of Custodial Bank Account for Shippers' Proceeds	3700
7002	Special Report Supplemental Balance Sheet	3410
7003	Special Report for Review of Dealer, Market Agency, and Packer Bonds	New
Combine w/ 3001&3	Annual Report of Clearing Agency	3200
Combine w/ 3001	Annual Report of Dealer – Short Form	3310
Discontinue	Special Report Statement of Accounts Payable for Livestock	3500
Combine w/ 7002	Supplemental Balance Sheet – Live Poultry Dealer	3610

For example, the redesigned annual report forms for livestock dealers, live poultry dealers, market agencies, and packers are respectively 3001, 3002, 3003, and 3004, with the form 3005 being

a supplemental annual report form only for packers with multiple plants.

The remaining three new forms are special report forms sent only when an event requires that the information be collected, with their 7000 level designation distinguishing special report status from annual report status. The new form 7001 is sent to market agencies suspected of violating the requirements of regulations for maintenance of custodial bank accounts. Form 7002 would be sent to any of the regulated entities when an insolvency violation, or other financial violation, is suspected. Form 7003, “Special Report for Review of Dealer, Market Agency, and Packer Bonds”, was created to establish the initial bond amount of businesses that register during the course of the year. Form 7003 reduced the initial data requirements for new entities, which in the past were required to complete the much longer annual report form.

Each of the new forms is divided into several sections. All the new forms have an initial *General Information* section and a final *Certification* section. The Information section contains contact information questions; one new question in the section is a request for the firm’s doing-business-as name. The Certification section contains a signature block and questions identifying the signer. Other sections vary based on the information required to regulate the type of business the forms are being sent to.

The second major step in the creation of CRU was to develop a new workflow process and procedures for processing the annual reports as part of the Business Process Re-engineering initiative. Under the new procedures, initial annual report processing will be performed by the CRU using the new PSAS application. The new PSAS management information system will generate mass mailings of annual report reminders. CRU staff will receive and respond to any filing date extension requests. CRU staff will determine if the reports are received when due. If not, CRU staff will generate and send a Notice of Default (NOD), stating that the report has not been received. CRU staff will track, scan, and record service dates for traceable delivery cards or other records.

If a response is not received, the CRU staff will notify the regional office to initiate a regulatory review of the business. After the regulatory review is assigned, reports received will be reviewed and processed by the assigned regional office agent.

When a report is received, the CRU staff scans, indexes, and routes the report for processing after performing a preliminary review to check for completeness, signature, and overall acceptability.

If unacceptable, CRU staff will generate and send a default notice via traceable mail, notifying the business that the report is not acceptable. As with late reports, CRU staff tracks whether the response is received within 30 days of the service delivery date of the notice. And as before, if the business does not respond, CRU staff will notify the affected regional office to initiate a regulatory review of the business, and revised reports received will be reviewed and processed by the assigned regional office agent.

If the report is acceptable, CRU staff will compare entity information in the database to determine if a name change, entity change, or change in owners or officers has occurred, and if so, send a request to the applicable regional office to update information or initiate a request for new or amended registration and further process the report.

The CRU staff will enter report data into the automated system and perform an analysis of the provided information. As part of the automated analysis, deficiencies will be identified. If there are no deficiencies the annual report is considered complete.

If deficiencies are found, such as insolvency, custodial shortage, procurement irregularities, or inadequate financial instruments (e.g., inadequate bond coverage), the CRU staff notifies the affected regional office unit supervisor to initiate the appropriate regulatory activity. The regional office will complete the regulatory activity and update the annual report database.

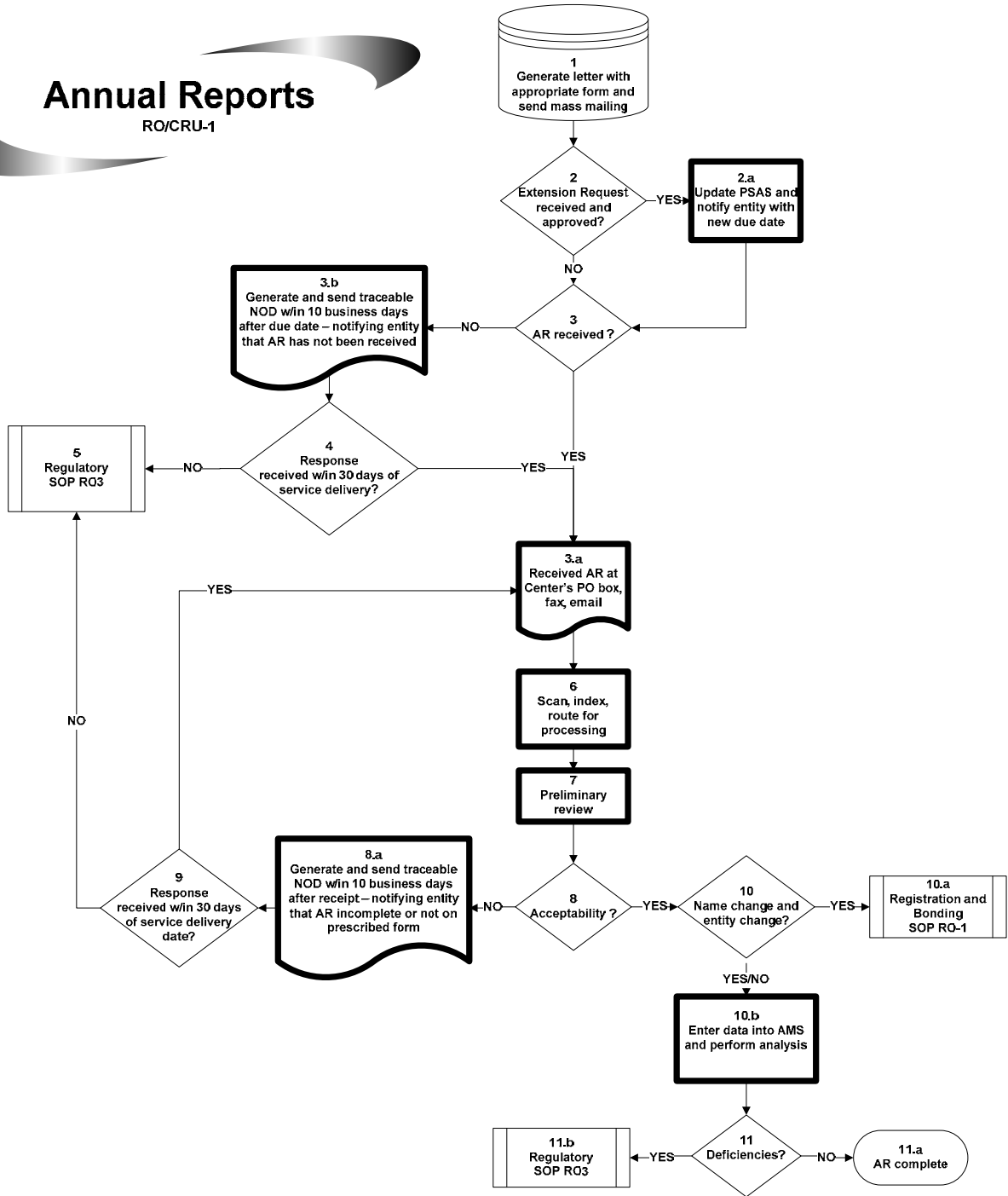
The CRU began collecting, processing, and analyzing the reports in January 2009. The regional office staff are responsible for performing followup report analysis (Figure 10).

The re-engineered annual reporting process using PSAS will allow P&SP to eliminate multiple handling, and much more efficiently perform preliminary analysis and work scheduling for report errors or reported violations that need to be investigated.

The CRU and new software will be fully functional in February 2009. Advanced enforcement analysis will be conducted regionally using electronic data generated by CRU in February 2009, and advanced policy analysis of the data will follow in April 2009.

Annual Reports

RO/CRU-1



AMS – Account Management System; AR – annual report; CRU – Central Reporting Unit; NOD – Notice of Default; PSAS – Packers and Stockyards Automated System; RO – regional office; SOP– standard operating procedure

Figure 10. Map of Workflow Process for Central Reporting Unit Located in Western Regional Office in Aurora, Colorado

ASSESSMENT OF THE INDUSTRIES

This section addresses three assessments of the regulated entities that P&SP conducts. First, it assesses the general economic state of the regulated industries, including trends in the number of firms in the regulated industries, statistics that measure financial conditions in the industries, and the percentage of the market held by the four largest firms of a particular sector (market concentration). Second, this section also examines the changing business practices of firms in the regulated industries, including pricing methods, particularly pricing on live weight versus carcass weight; procurement methods, especially 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 the concerns.

The data for 2008 suggest an increase in the number of firms regulated by P&SP compared to 2007, which is likely a result of the transition P&SP initiated in 2008 to a new database system and entity identification process. Despite the change in recorded data patterns, however, the real number of entities subject to the P&S Act likely will continue to trend downward. As firms exit without replacement, there is a tendency for the larger firms to increase their share of the market.

The four largest slaughter firms' share of the total value of livestock purchases (i.e., aggregate industry concentration) has, however, declined slightly during the last 4 years to around 65 percent. Patterns of concentration in the purchase of different types of livestock, however, have exhibited varying trends. Four-firm concentration ratios by volume of steer and heifer slaughter and boxed beef production have been relatively stable in recent years, although boxed beef concentration declined in 2007.

Concentration in poultry slaughter has trended upward since 2000. Cow and bull slaughter concentration increased from 1997 to 2007. Concentration in hog slaughter increased sharply in 2003, but has been stable since except for a decline in 2006 followed by a return to the previous level in 2007. Concentration in sheep slaughter declined from 1998 through 2004, but has increased sharply since.

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. The results of expanded plant capacities have been lower-cost products for consumers and better income margins for producers and processors.

In late 2008, firms regulated under the P&S Act may be exiting business at rates above longer-term trends. The faster rates of economic contraction are due to high feed and energy costs in the late summer of 2008 and restricted access to credit in the fall, both of which contributed to weakening domestic and international demand for livestock and meat products.

If the business conditions at the end of 2008 worsen and persist into 2009, industry contraction is almost certain to lead to greater concentration rates. These rates would likely be above those seen in the past due to consolidation from the adoption of cost-saving technologies.

Greater consolidation due to overall economic contraction would likely impact the balance of power among competing businesses, market access for livestock sellers, and prices paid by consumers, producers, and processors. Such contraction also would unfold in unpredictable ways. For example, economic shocks may affect industry conditions relative to one species more than another depending on consumer demand, or the effect may favor one region of the country more than another by altering relative cost-of-production patterns in the affected regions.

Business practice trends also will continue to shift. Carcass-basis purchases of cattle and hogs increased early in the decade and have stabilized around 19 million head for cattle and 80-85 million head for hogs. Carcass-based purchases reflect a trend by packers to pay livestock sellers through methods tied to product values.

As the volume of carcass-based procurement has increased, packers have increased the development and testing of carcass evaluation devices in the beef industry. Changes to carcass merit programs for hogs were not significant in 2007, perhaps reflecting the fact that carcass-basis pricing of hogs has stabilized at high levels in recent years as packers have become satisfied with the current degree of leanness in hogs.

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. The trends will be resistant to change, even if there is significant economic deterioration in 2009, 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 2006 and 2007, but packer feeding and use of marketing agreements remain near levels seen in 2000. Forward contracts and packer feeding each continue to represent relatively small portions 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.

General Economic State of the Industry

At the end of 2008, 339 bonded livestock slaughter firms, 126 live poultry dealers, 4,685 registered dealers, and 1,326 market agencies were determined to be subject to the Act (Table 17).

Entities subject to the Act are:

- Bonded slaughter firms include federally inspected and non-federally inspected plants. 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 livestock for slaughter of \$500,000 or more 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 defined as entities engaged in the business of buying or selling livestock in commerce on a commission basis, furnishing stockyard services, or, in rare cases, a non-business 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; that integrator then will slaughter and further process the poultry.

- Posted stockyards are physical facilities, and are not necessarily separate businesses. For example, county fairgrounds may be registered as a stockyard. Terminal markets and auction markets are located at stockyards.

Table 17. Number of Slaughterers, Live Poultry Dealers, Bonded Dealers and Market Agencies, and Posted Stockyards Subject to the P&S Act

Year	Bonded slaughter firms	Live poultry dealers	Bonded dealers	Bonded market agencies	Posted stockyards
1999	386	N/A	4,877	1,700	1,548
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	339	126	4,685	1,326	1,392

In 2008, P&SP began a transition 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 will de-post 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 value of bonds held by packers has trended upward with the increase in dollar volume of business, while the value of bonds held by other types of entities has remained relatively constant (Figure 11 and 12). The total value of bonds held by subject firms should continue to follow the trend in the total dollar business volume of these firms.

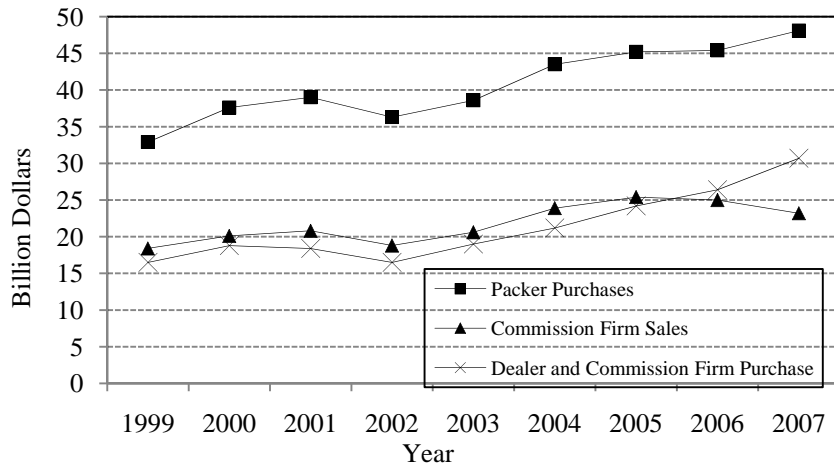


Figure 11. Dollar Volume of Slaughter Firms, Dealers, and Market Agencies Selling and Buying on Commission Subject to P&S Act, 1999-2007

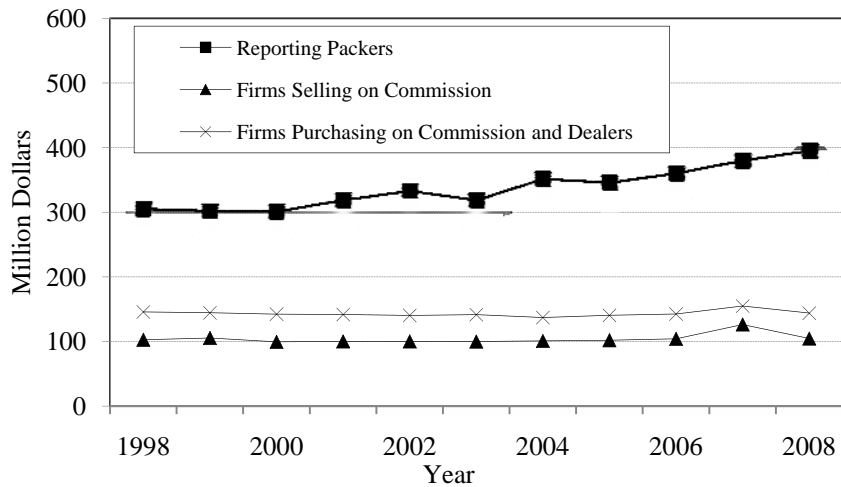


Figure 12. Value of Bonds Held in Accordance With P&S Act by Slaughter Firms, Market Agencies Selling on Commission, and Dealers and Market Agencies Purchasing on Commission, 1998-2008

The four largest slaughter firms’ share of total industry expenditures on livestock for slaughter increased between 1997 and 2003 but with downturns in 2001 and 2002, and has declined the past 4 years (Figure 13).

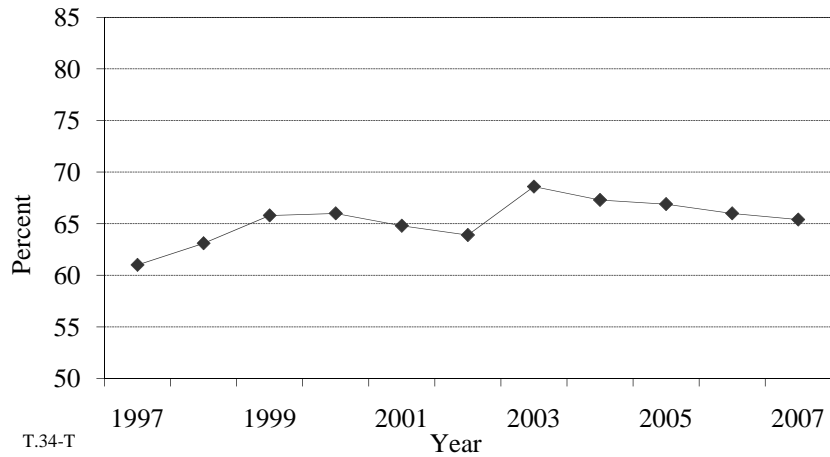


Figure 13. Share of Total Industry Livestock Procurement Expenditures for the Four Largest Slaughter Firms, Ranked by Total Livestock Procurement Expenditure

While concentration has generally increased since 1980, changes in recent years have varied somewhat across livestock types (Table 18).

Table 18. Four-Firm Concentration as Percent Market Share of Livestock Slaughter by Type of Livestock, Selected Years, 1980-2007

Year	Steers & Heifers	Boxed Beef	Sheep & Lambs	Hogs
	Percent			
1980	36	53	56	34
1995	81	84	72	46
2000	81	85	67	56
2001	80	84	66	57
2002	79	83	65	55
2003	80	84	65	64
2004	79	82	65	64
2005	80	83	70	64
2006	81	84	68	61
2007	80	80	70	65

Note: Values are based on calendar year federally-inspected slaughter except for 1980 and figures for all years for boxed beef, which are based on firms' fiscal years as reported to P&SP.

Concentration of the four largest steer and heifer slaughterers rose from about 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. 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 to 70 percent in 2007.

Four-firm concentration has stabilized in recent years, overall and by type of livestock. Current economic conditions may influence future changes in the livestock and meat industry.

Two financial ratios are used to summarize financial conditions in the meat-packing industry (Table 19). The *Operating Profit Margin*, computed as operating income (gross profit minus operating expenses) divided by total revenue, measures the proportion 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 19. Average Profit Margin and Current Ratios for the Top 4 and the Top 20 Firms

Year	Profit Margin		Current Ratio	
	Top 4	Top 20	Top 4	Top 20
2006	-0.2	0.8	1.9	1.3
2007	0.5	1.7	1.9	1.6

Profit margins for the 4 largest firms moved from slightly negative in 2006 to slightly positive in 2007, and also improved for all of the 20 largest firms. The Current Ratios for the largest 4 remained constant in 2006 and 2007, but improved slightly for the entire group of 20 largest firms. Current economic uncertainties likely will negatively affect both of these ratios.

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, 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, whereas many smaller packers specialize in cow and bull slaughter and almost no steers and heifers.

Note also that 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 over the past 10 years but increased in 2006 and 2007 (Figure 14). 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.

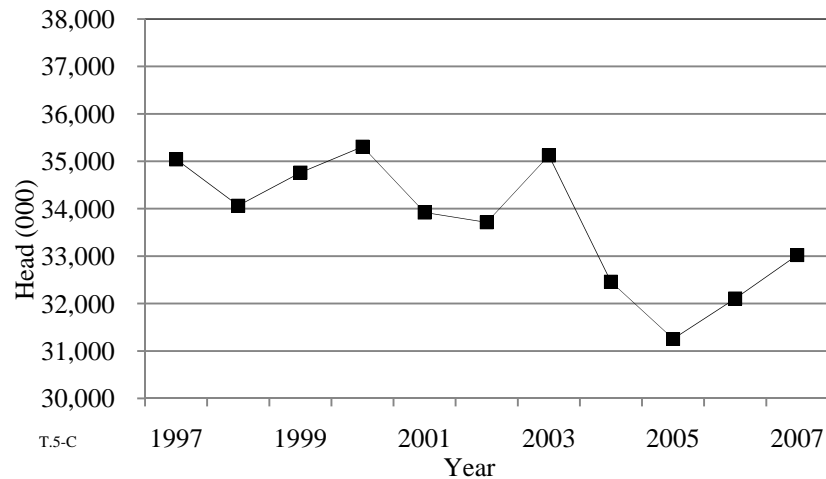


Figure 14. Total Slaughter Cattle Purchases for Firms Reporting to P&SP

The number of plants reporting to P&SP declined by approximately 100, or 38 percent, from 1997 through 2003, as plant sizes increased and smaller plants closed (Figure 15). The number was about the same in 2007 as in 2003, declining after a small increase in 2004. This gradual reduction in total numbers is expected to continue as persistent economic troubles accelerate firm closures.

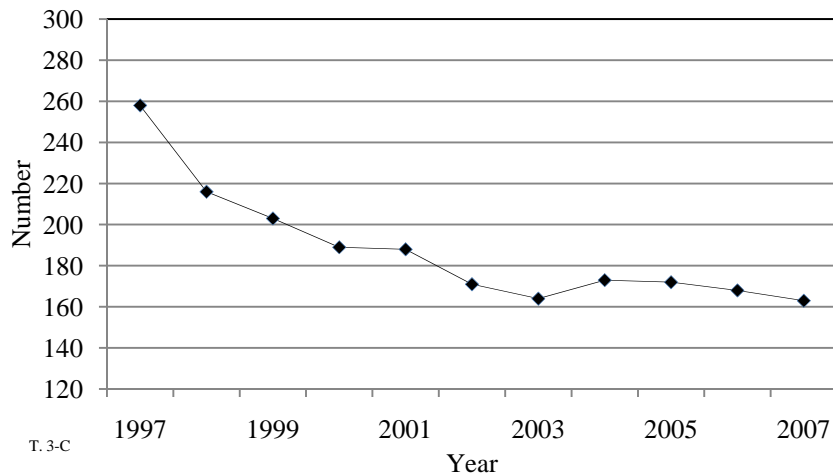


Figure 15. Number of Cattle Slaughter Plants for Firms Reporting to P&SP

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 1997. The share of boxed beef production has moved with slaughter concentration, although slightly higher until 2007 (Figure 16).

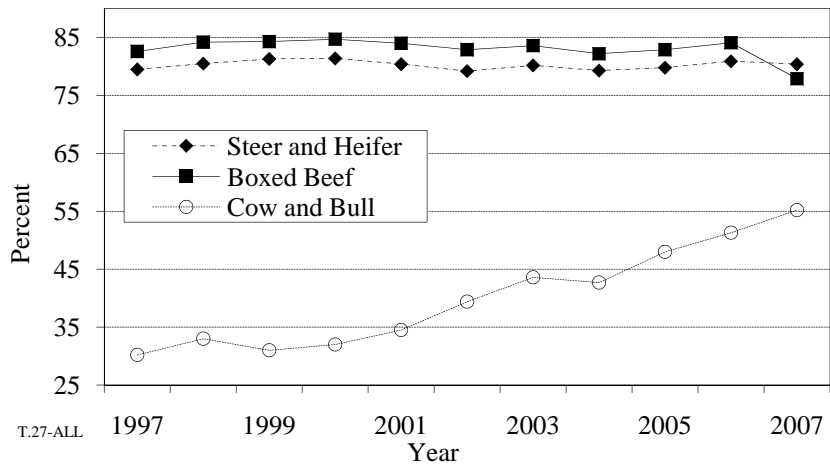


Figure 16. Combined Market Share (by Volume) for the Four Largest Steer and Heifer Slaughter Firms, Four Largest Cow and Bull Slaughter Firms, and Four Largest Boxed-Beef Producers

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, with some smaller plants being acquired by larger firms. These factors have 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 in the patterns due to uncertainties about developments in the overall economy beginning 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 17). Total purchases for slaughter are expected to remain steady.

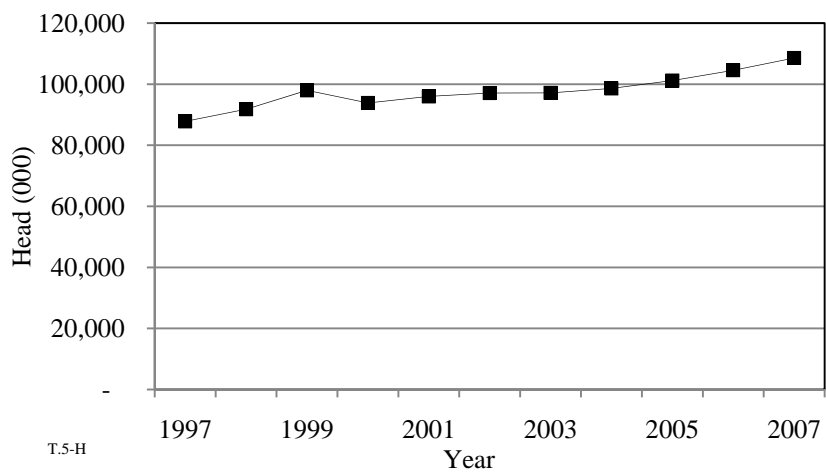


Figure 17. Total Hog Purchases for Slaughter for Firms Reporting to P&SP

The number of plants has been stable since 2004, and likely will remain so unless economic conditions decline further in 2009 (Figure 18).

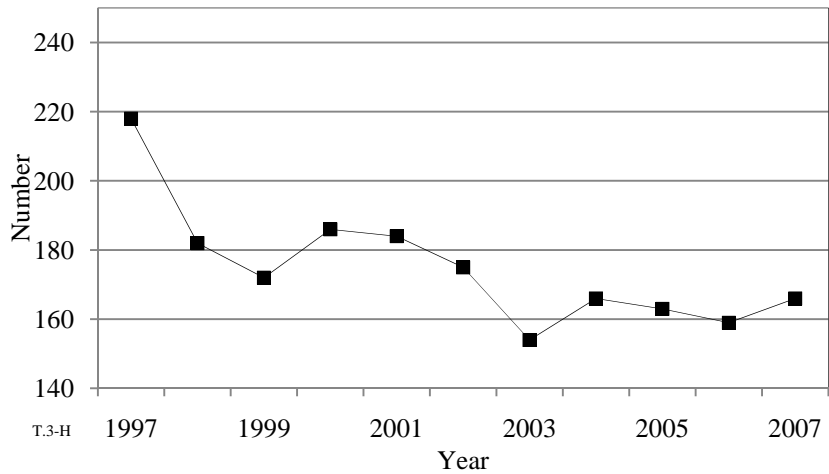


Figure 18. Number of Hog Slaughter Plants for Firms Reporting to P&SP

The four-firm concentration ratio for hog slaughterers was roughly 55 percent in the late 1990s and then increased in 2003 to near 65 percent where it remained through 2007 except for a 1-year decline in 2006 (Figure 19). Future concentration will likely remain near the present level.

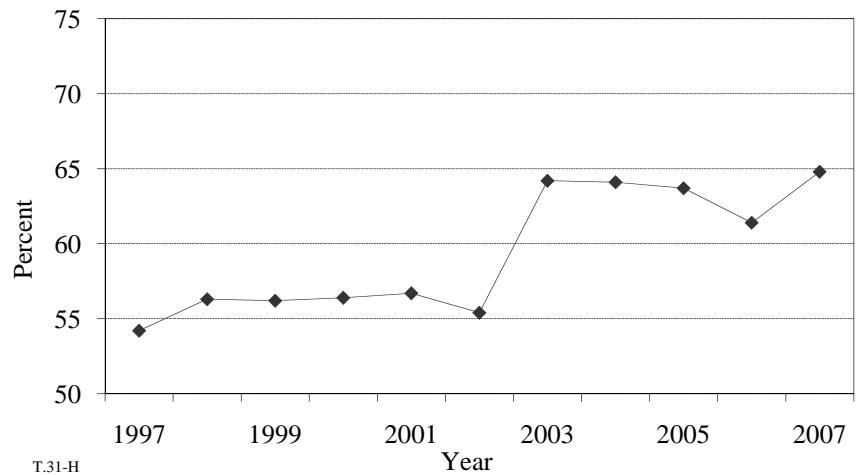


Figure 19. Combined Market Share (by Volume) for the Four Largest Hog Slaughter Firms

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 two between 1997 and 2005, remained relatively constant in 2006, then increased in 2007 (Figure 20). Annual slaughter of sheep and lambs will likely

remain in the 2.0 million to 2.5 million head range in the future, with a small decline in 2008.

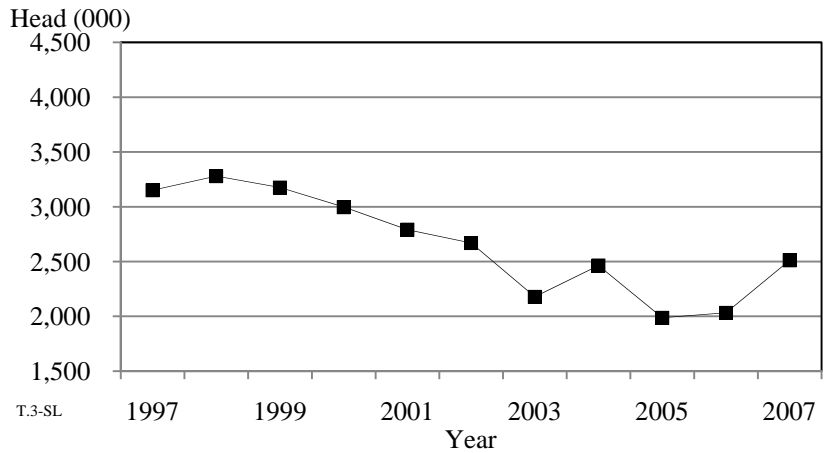


Figure 20. Total Slaughter Sheep and Lamb Purchases for Firms Reporting to P&SP

The number of plants slaughtering sheep and lambs declined steadily from 1997 through 2002, but has remained relatively constant through 2007 and is expected to continue near present levels (Figure 21).

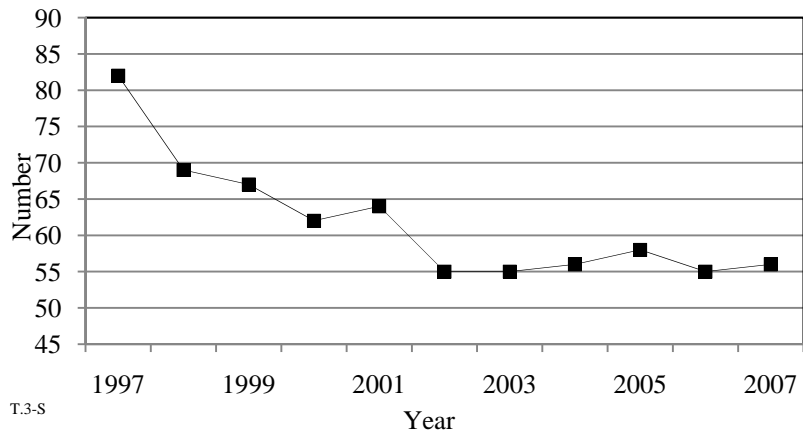


Figure 21. Number of Sheep and Lamb Slaughter Plants for Firms Reporting to P&SP

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 22).

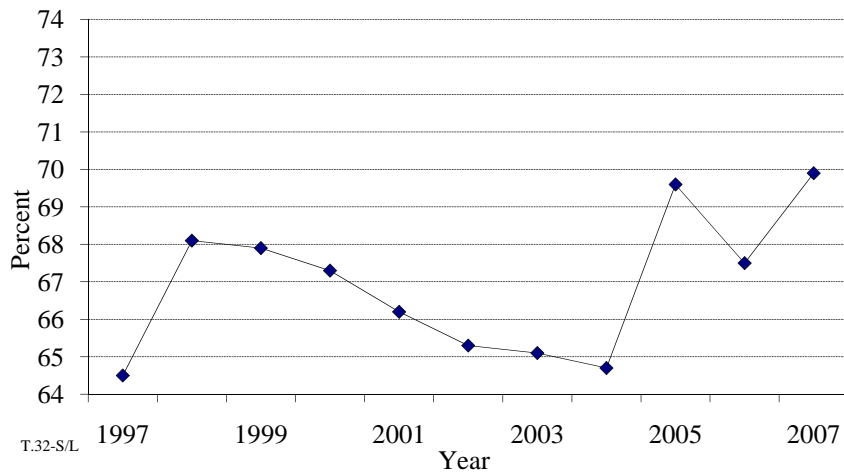


Figure 22. Combined Market Share (by Volume) for the Four Largest Sheep and Lamb Slaughter Firms

Due to the small total slaughter of the industry, relatively moderate volume adjustments among any of the largest four firms result in relatively large changes in the percent of total industry slaughter accounted for by those firms. For example, in 1998, a new large firm entered the industry as a new member of the group of four largest, and increased the share of the top four. 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 declined in 2006, returning to 2005 levels in 2007, but as in previous years these changes in shares represented only a few thousand head of slaughter. 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

Beginning with this reporting year, P&SP will provide slaughter volume, industry concentration, and two measures of live poultry dealer financial health (the net profit margin and current ratio) obtained from annual reports the industry files with P&SP.

In 2007, 45.6 billion pounds of poultry were reported to P&SP as slaughtered. By comparison, in 2006 the federally inspected (FI) volume was 35.7 billion pounds. This reflects 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, but continued to show an upward trend in 2007, with firms reporting 6.4 billion pounds to P&SP compared to the FI volume for 2006 of 5.7 billion pounds. Poultry slaughter volume was maintained at a relatively high rate 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 2007, the four largest broiler slaughterers controlled about 57 percent of the market share and the four largest turkey slaughterers controlled 52 percent. In contrast, in 2000, the four largest broiler slaughterers controlled roughly 50 percent of the market and the four largest turkey processors about 41 percent. Concentration is expected to remain relatively stable at 2007 levels into 2009.

In 2007, operating profit margin (the proportion of revenue from sales that remains after production costs have been paid for) of the 20 largest broiler companies averaged 4.8 percent and was 2.4 percent for the 20 largest turkey processing companies (Table 20).

Table 20. Poultry Industry Market Share, Profit Margin, and Current Ratio.

Type	Market Share %	Profit Margin		Current Ratio	
		Top 4	Top 20	Top 4	Top 20
Broiler	57	3.5	4.8	2.9	2.5
Turkey	51	5.0	2.4	1.7	2.4

The average profit margins of the 4 largest turkey firms was higher than that of the entire group of 20 largest, while for broilers profits averaged lower for the 4 largest than for the entire group of 20. For turkey firms, the 4 largest exhibited less liquidity than the group of 20 largest, while the 4 largest broiler slaughter firms exhibited higher liquidity than the entire group of 20 largest.

Profit margins and liquidity in the poultry industry have been subject to considerable negative pressure in late 2008 from weakening export markets and tight credit markets. Because of the lower cost of poultry production relative to pork and beef, poultry firms may be less vulnerable if current economic conditions persist for any length of time and domestic consumers select lower-cost proteins.

Changing Business Practices

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 is illustrated by a greater decline since 1997 in the number of firms slaughtering two or more classes of livestock than in the number of firms slaughtering a single class (Figure 23).

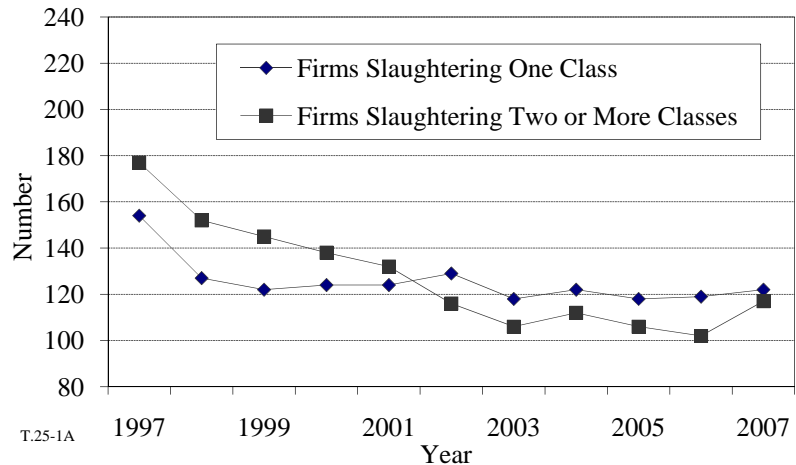


Figure 23. Number of Firms Slaughtering One Class and Number of Firms Slaughtering Two or More Classes of Livestock

For purposes of this comparison, the separate classes of livestock are steers and heifers; cows and bulls; calves; sheep and lambs; and hogs. The decline in number of firms, however, has followed similar patterns for all types for the last few years with some stability since 2003, and recent patterns are expected to continue.

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. In livestock, and cattle transactions in particular, pricing methods are most often divided into two categories: live-weight or 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 (for example, 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 most of the 1980s and 1990s, the proportion of cattle purchased on a live-weight basis by packers reporting to P&SP has not shown a steady pattern since 2004 (Table 21).

Table 21. Number and Percentage of Cattle Purchased Live-Weight and Carcass-Weight by Packers Reporting to P&SP, 1997-2007

Year*	Live-weight		Carcass-weight	
	Head (000)	Percent	Head (000)	Percent
1997	18,413	52.5	16,628	47.5
1998	19,049	55.9	15,016	44.1
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

The total volume of cattle purchased on a carcass basis, as opposed to on a live-weight basis, trended upward from 1998 through 2002 (Figure 24). Following a sharp decline in 2004, the volume stabilized in 2005 and 2006 then increased in 2007. The proportion of cattle purchased on a carcass basis is expected to remain in the 57-62 percent range.

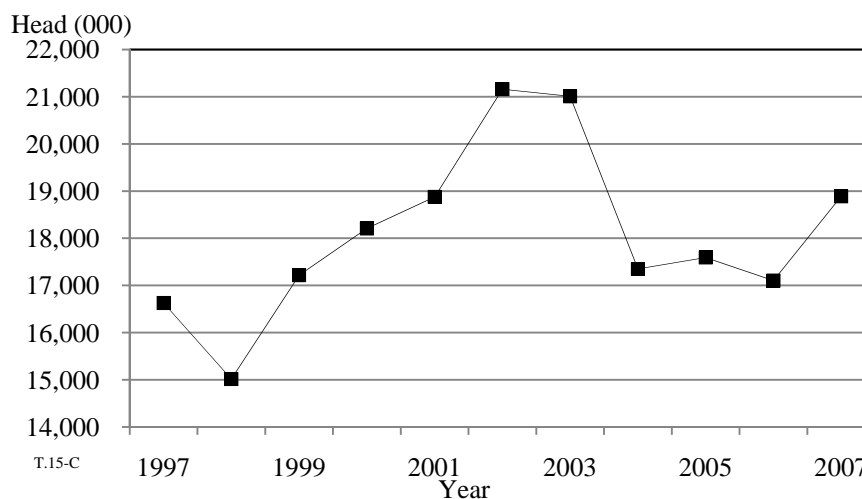


Figure 24. Cattle Purchases on a Carcass Basis

The proportion of calves purchased on a carcass-weight basis was about the same in 2007 as in 1997, but has exhibited a mixed pattern in recent years. Having declined from 2000 through 2003, the proportion of calves purchased on a carcass basis increased considerably in 2004 then decreased in 2005 (Table 22). It is expected that data will show the proportion remained near 40 percent in 2008.

Table 22. Number and Percentage of Calves Purchased Live-Weight and Carcass-Weight by Packers Reporting to P&SP, 1997-2007

Year*	Live-weight		Carcass-weight	
	Head (000)	Percent	Head (000)	Percent
1997	734	59.5	500	40.5
1998	656	56.6	504	43.4
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

* See Table 18 footnote.

Packers have increased the development and testing of carcass evaluation devices in the beef industry. P&SP personnel participate in carcass tests conducted jointly by the USDA 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 25).

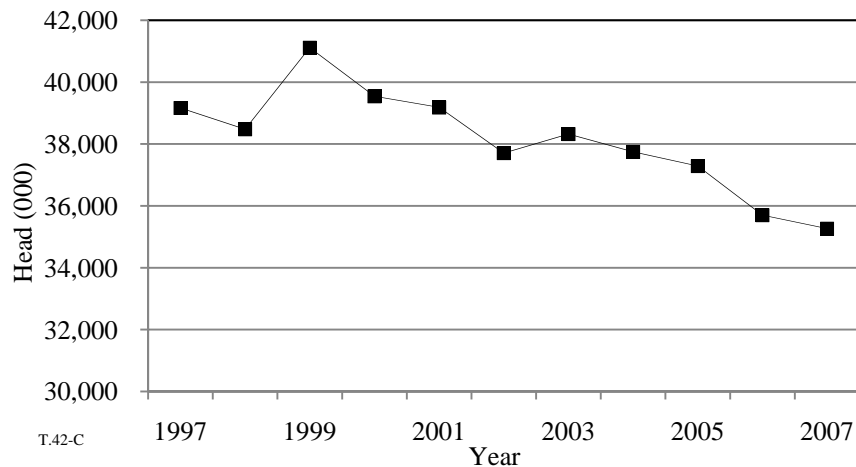


Figure 25. Volume of Cattle (Slaughter and Non-Slaughter) Marketed Through Firms Selling on Commission

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 sales for immediate delivery or a delayed delivery, normally

within 2 weeks, 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.

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, P&SP expanded its collection to include data from the five largest fed cattle slaughter firms. The firms use packer feeding, forward contracts, and marketing agreements to procure cattle for delayed delivery. Data show that packers’ overall use of types of committed procurement increased in the early 2000s, declined as a percent of their total slaughter in 2003 and 2004, then increased again in 2006 and 2007 (Figure 26). Prior to 2006, data refer to the four largest firms. In 2006 and 2007, data include the five largest firms.

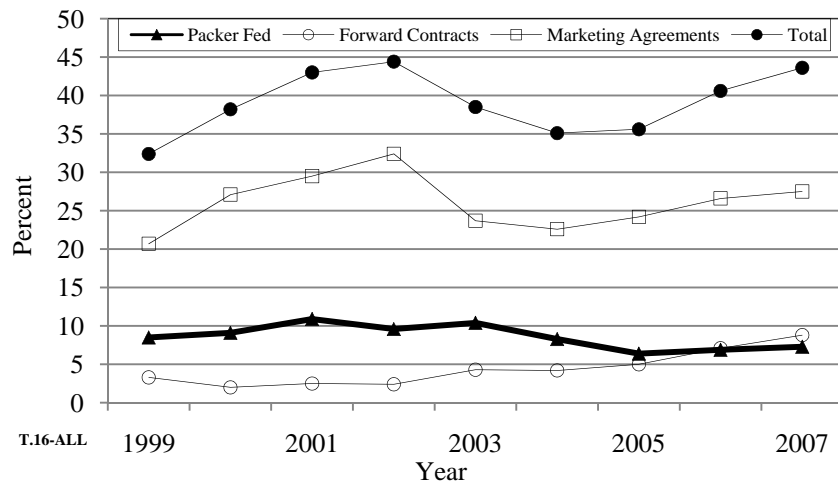


Figure 26. Percentage of Steers and Heifers Procured Through Alternative Types of Committed Procurement Arrangements by the Four (Five) Largest Steer and Heifer Slaughter Firms

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 are obtained through packer feeding arrangements by the largest steer and heifer slaughter firms declined in 2004 and 2005, but increased slightly in 2006 and 2007.

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, e.g., using prices from the Chicago Mercantile Exchange futures market for live cattle with an adjustment for the basis 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 have trended upward since 2004, but remains under 10 percent of total procurement.

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 from 2005 through 2007.

Overall, there was a 3.3 percentage point increase in total committed procurement (packer feeding, forward contracts, and marketing agreements) by the five largest steer and heifer slaughter firms in 2007. The recent trends will likely continue, with small further increases in use of marketing agreements but relatively stable use of other methods.

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 reopenings 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 review is the responsibility of either the U.S. Department of Justice 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.

In 2008, there were significant changes in business practices in the cattle processing sector. Tyson Foods, Inc. made several adjustments in its operations. It ceased livestock slaughter at its Emporia, Kansas, plant in February 2008, but continued to use the facility for cold storage and further processing. Tyson also closed its beef and pork processing plant in York, Nebraska, in June 2008. Finally, Tyson entered an agreement to sell its beef slaughter plant in Brooks, Alberta, Canada, to XL Foods, Inc. in June 2008.

In March 2008, the packing firm JBS SA (JBS) announced the proposed acquisition of National Beef Packing Company, LLC (National); Smithfield Beef Group, Inc. (SBG); and Five Rivers Ranch Cattle Feeding, LLC (Five Rivers). DOJ filed a lawsuit on October 20, 2008, to block JBS's purchase of National. On October 23 JBS announced it had completed the acquisition of SBG and Five Rivers. With the acquisition, JBS obtained slaughtering plants in Green Bay, Wisconsin; Plainwell, Michigan; Souderton, Pennsylvania; and Tolleson, Arizona. JBS also acquired feedlots in Malta, Idaho; Gilcrest, Colorado; Kersey, Colorado; Yuma, Colorado; Lamar, Colorado; Ulysess, Kansas; Texhoma, Oklahoma; Hartley, Texas; and two feedlots in Dalhart, Texas.

Meyer Natural Angus acquired Coleman Natural Foods in Limon, Colorado, in June 2008. The deal included B3R Natural Meats in Childress, Texas. Meyer closed the slaughter plants in Childress and Limon, and a processing plant in Denver, Colorado.

Hallmark Meat Packing Co., Inc. in Chino, California, closed in January 2008. The plant was sold and reopened as American Beef Packing, Inc., which commenced slaughter operations in November 2008.

AgriProcessors, Inc. of Postville, Iowa, filed for bankruptcy in November 2008.

Cargill Meat Solutions Corp.'s further processing plant in Booneville, Arkansas, was destroyed by fire on March 23, 2008. Cargill later announced it will not rebuild the plant.

Hogs—Changing Business Practices

The proportion of hog 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 (Table 23; Figure 27). The proportion of hogs purchased

on a carcass basis likely will remain between 75 and 80 percent of total hog slaughter.

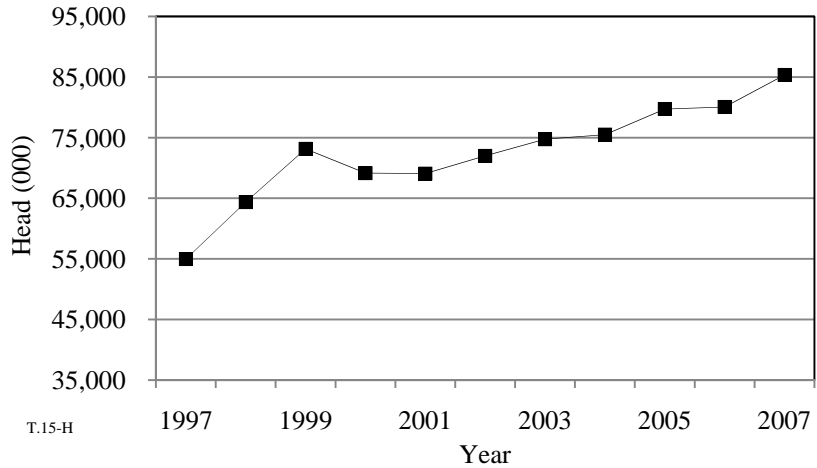


Figure 27. Hog Purchases on a Carcass Basis

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 23. Number and Percentage of Hogs Purchased by Live-Weight and Carcass-Weight for Packers Reporting to P&SP, 1997-2007

Year	<u>Live-weight</u>		<u>Carcass-weight</u>	
	Head (000)	Percent	Head (000)	Percent
1997	32,821	37.4	54,978	62.6
1998	27,448	29.9	64,383	70.1
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

The volume of hogs marketed by firms selling on commission declined between 1998 through 2002 (Figure 28). The volume of hogs marketed through commission firms has trended upward

since 2002, and future changes will likely follow the pattern since 2002.

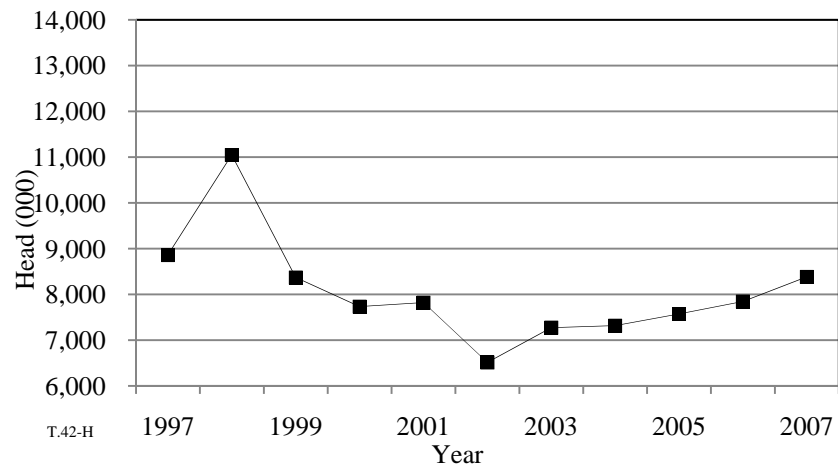


Figure 28. Volume of Hogs Marketed Through Firms Selling on Commission

Like cattle packers, hog packers use multiple procurement methods. About 90 percent of hogs are obtained on a “committed procurement” arrangement at least 14 days prior to slaughter. About 45 percent of hogs procured are delivered under a marketing agreement. 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. “Packer-fed” hogs are supplied from a packer-owned farrowing operation, and are often fed under contract for the packer. “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 an expiring 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, marketing agreements, forward contracts, and spot market procurement. Among multi-plant packers, these combinations may vary by plant.

In fiscal year 2004, P&SP implemented a Web-based Swine Contract Library (SCL) in accordance with the requirements of the Livestock Mandatory Reporting Act of 1999 (LMRA). The LMRA expired briefly in the fall of 2004 but was extended for 1 year. During the 2004 period when the Act had expired, about half of the plants reported to P&SP on a voluntary basis, accounting for a

large decline in late 2004 (Figure 29). Normal reporting resumed during the 1-year extension. Since the LMRA's subsequent expiration in September 2005, approximately half the previously responding plants continued reporting to P&SP on a voluntary basis, but the number has declined since then to about one-third of the plants.

The SCL reports swine contract information from swine (hog) packing plants with a slaughter capacity of 100,000 or more swine per year. The SCL reports information about the submitted contracts by region, including price, premiums, discounts, grids, formulas, and other important contract terms that P&SP extracts from offered and available contracts that packing firms use to purchase hogs. Each month, the SCL also reports estimates of total future deliveries of hogs under contract for the following 6- and 12-month periods. The SCL data are known in advance of AMS data on actual deliveries and thus provide a forecast estimate.

Prior to the expiration of the LMRA, P&SP found that packers' reports to the SCL of estimated future deliveries under contract tended to underestimate actual deliveries subsequently reported by AMS, but still provided a useful indication of the trend in deliveries. When reporting to the SCL and AMS became voluntary in September 2005, fewer plants provided data to the SCL about estimated future deliveries under contract than those that voluntarily provided data to AMS about actual deliveries. As a result, SCL estimates became a less accurate trend predictor (Figure 29).

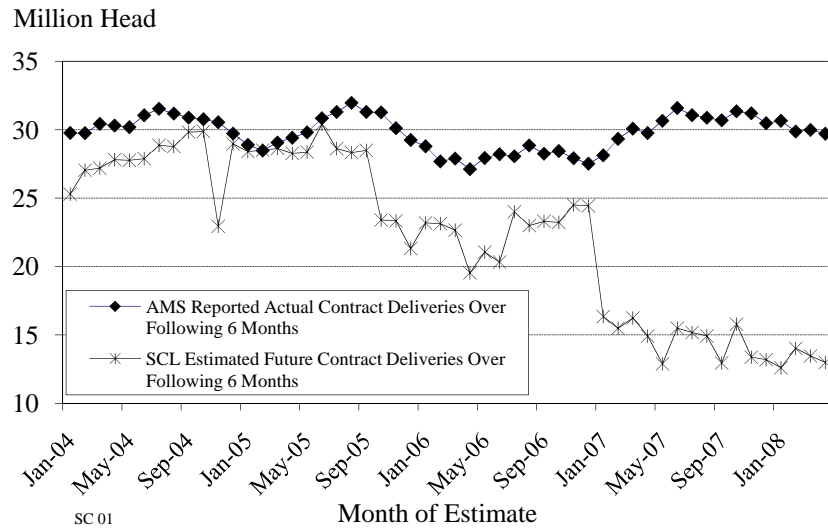


Figure 29. Estimated Future Contract Hog Deliveries Compared to Actual Contract Deliveries During the Same Period, National Totals, All Contract Types

In October 2006, the LMRA was again renewed, including the SCL provision. However, submission of contract information continues to be voluntary until P&SP regulations to implement the LMRA are issued. P&SP expects that the relationship between estimated and actual deliveries should approach a more consistent pattern once all packers resume filing reports to the SCL as required.

In 2008, there were no significant hog processing plant closures, acquisitions, or mergers.

Sheep—Changing Business Practices

The volume of sheep and lambs purchased on a carcass basis peaked at over 1.9 million head in 2001, but has declined to around 1 million head in recent years (Figure 30). The decline in carcass purchases has corresponded to the decline in total slaughter over time, so data will probably show that purchases of sheep and lambs on a carcass basis declined slightly in 2008, given the expected small decline in total volume of sheep and lamb slaughter noted above.

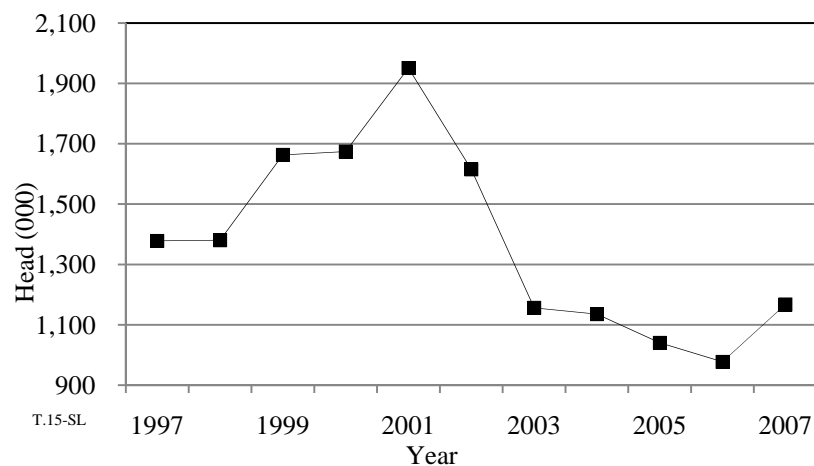


Figure 30. Sheep and Lambs Purchased on a Carcass Basis

Live-weight purchases continue to account for around half of the sheep and lamb purchases for slaughter by packers reporting to P&SP (Table 24).

Table 24. Number and Percentage of Sheep and Lambs Purchased by Live-Weight and Carcass-Weight for Packers Reporting to P&SP, 1997-2007

Year*	<u>Live-weight</u>		<u>Carcass-weight</u>	
	Head (000)	Percent	Head (000)	Percent
1997	1,773	56.3	1,378	43.7
1998	1,899	57.9	1,380	42.1
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

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 followed a downward trend similar to the trend in use of commission firms for cattle, and this will likely continue (Figure 31).

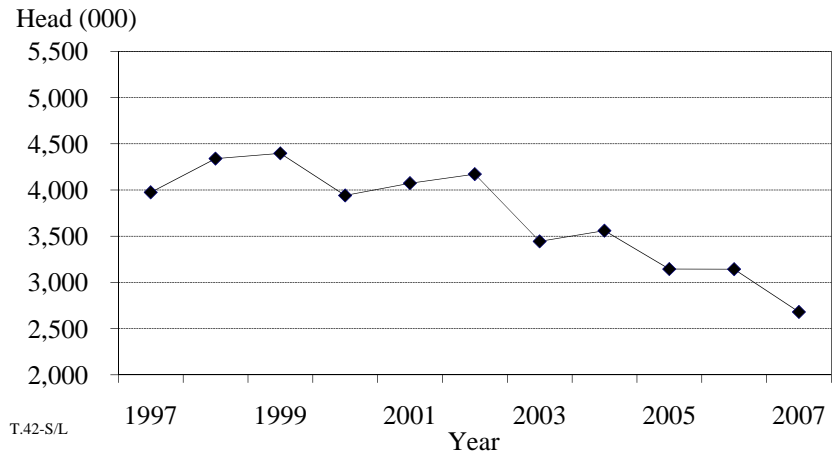


Figure 31. Volume of Sheep Marketed Through Firms Selling on Commission

Poultry—Changing Business Practices

Poultry firms have recently experienced considerable difficulties due to oversupply of meat, high prices for inputs, and weak domestic and international demand.

In March 2008 Hain Pure Protein Corporation acquired the turkey production facility and distribution center of Pilgrim's Pride Corporation in New Oxford, Pennsylvania. At the same time Hain created a new, wholly owned subsidiary from the acquisition, New Oxford Foods, LLC. The acquisition ended Pilgrim's Pride Corporation turkey slaughtering.

Pilgrim's Pride followed with poultry production cutbacks during the second half of fiscal 2008, the closure of a plant in Siler City, North Carolina, and seven distribution centers, and transfer of tray-pack operations from its El Dorado, Arkansas, plant to six other case-ready sites. In August 2008, Pilgrim's Pride announced plans to idle a chicken processing plant in Clinton, Arkansas, and a further-processing facility in Bossier City, Louisiana. On December 1, 2008, the company, along with several of its wholly owned subsidiaries, announced that, in an effort to address certain short-term operational and liquidity challenges, it was filing a voluntary petition for relief under Chapter 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the Northern District of Texas.

Industry Concerns

This section identifies concerns expressed by producer and other interested parties to Congress, which then through legislation directed P&SP to promulgate regulations, or concerns P&SP has about particular industry practices. In each case the concern is stated and the actions P&SP is taking to address the concern are described.

Transparency of Market and Dealer Information

Concern: Livestock sellers have indicated to P&SP that they have difficulty obtaining information about the schedules of rates and charges for services provided by stockyards (tariff schedules) and bond protection levels carried by livestock dealers, markets, and packers. This is nonproprietary information that should be readily available to sellers.

P&SP Action: To facilitate improved access to public information about businesses regulated under the P&S Act, in 2008 P&SP initiated postings on its public Web site of the bond levels carried by regulated entities, and is exploring the potential for listing tariff information.

Production Contract Requirements

Concern: Certain production contracts do not allow reasonable times for a producer to cancel a new contract.

P&SP Action: Production contract provisions in Section 11005 of the Food, Conservation, and Energy Act of 2008 (Farm Bill) provide a producer the right to cancel a production contract within 3 days or any other time period specified in the contract; require disclosure of the termination provisions of the contract; and require that each contract must disclose if additional capital investments may be required during the life of the contract. The Farm Bill also requires that resolutions of production contract disputes shall be located in the Federal judicial district in which the principle part of business takes place. Further, the Farm Bill provides that production contracts may specify which State law applies if there is a dispute under the contract, unless that practice is prohibited by State law in which the principle part of the contract performance takes place. The law also requires production contracts that mandate arbitration to allow the producer to decline to be bound by that provision. The law provides that a livestock or poultry

producer has the right to arbitration if both parties agree in writing after a dispute arises.

Section 11006 directs the Secretary to promulgate regulations to establish criteria that the Secretary will use in determining what would constitute an unreasonable preference or advantage; what would constitute adequate notice to poultry growers of suspension of delivery of birds; when an additional capital investment requirement would constitute a violation; and what would constitute a reasonable period of time for a live poultry dealer or swine contractor to provide to remedy a breach of contract that could lead to contract termination. P&SP held three listening sessions in Arkansas, Iowa, and Georgia, and based on input from these sessions and other available information is proceeding with development of necessary regulations.

Adding Swine Contractors to Certain Existing Regulations

Concern: Swine contractors were not included in the list of regulated entities subject to specific regulations under the P&S Act. The Farm Security and Rural Investment Act of 2002 (Pub. L. 107– 171) amended the P&S Act to define and add “swine contractors” as a regulated entity. New regulations are necessary to implement this amendment.

P&SP Action: P&SP is adding “swine contractors” to the list of regulated entities subject to specific regulations under the P&S Act that prohibit regulated entities from circulating misleading reports about market conditions or prices. P&SP is also amending regulations that address inspection of business records and facilities, information that regulated entities are required to share with the Secretary of Agriculture, and USDA’s responsibility to refrain from unauthorized disclosure of that information. Including swine contractors under specific regulations under the P&S Act will clarify that the regulations apply to swine contractors and swine production contract growers and make it easier for P&SP to enforce the provisions of the P&S Act and regulations. P&SP published a Notice of Proposed Rulemaking in the *Federal Register* on October 21, 2008.

(<http://archive.gipsa.usda.gov/rulemaking/fr08/10-21-08a.pdf>)

Dealer and Market Agency Registrations Under the P&S Act

Concern: Current section 201.10 of the P&S Act sets no time limits on registration, so once an entity registers it remains registered indefinitely. As regulated entities exited from business,

or changed ownership or a business name, the rule allowing indefinite registrations made it difficult, if not impossible, for P&SP to maintain accurate rolls of regulated entities.

P&SP Action: P&SP is amending existing regulations (9 CFR 201.10) to establish 5-year registration terms for market agencies and dealers operating subject to the P&S Act. Under current regulations, there is no expiration date or renewal process for the registration of a market agency or dealer. The proposed amendment will help P&SP better regulate the business operations of market agencies and dealers through the effective enforcement of the P&S Act. P&SP published a Notice of Proposed Rulemaking in the *Federal Register* on December 16, 2008. (<http://archive.gipsa.usda.gov/rulemaking/fr08/12-16-08.pdf>)

Poultry Contracts; Initiation, Performance, and Termination

Concern: Due to vertical integration and high concentration in the poultry industry, growers have little negotiating power regarding contract terms and often receive contracts on a “take-it-or-leave-it” basis. They often cannot contract with an alternate poultry company on more favorable terms because no feasible alternatives are nearby. Growers are at a further disadvantage because they may not grasp the full content of their own contracts, and have been constrained by confidentiality clauses from discussing contracts with business advisers. At the same time, poultry companies have detailed information about the market as a whole and about the current terms being offered to other growers. There is considerable information asymmetry as well as an imbalance in market power in much poultry contracting, creating significant potential for poultry companies to engage in unfair and deceptive practices.

P&SP Action: P&SP is proposing regulations to amend Section 201.100 to require that: (1) the growout contract shall be delivered to the grower in writing at the same time that the grower is provided with specifications for the poultry houses that must be used for the contract; (2) the growout contract shall include the criteria that will be used to place the grower on a performance improvement plan; (3) a grower shall be notified in writing 30 days before removal of the current flock that a contract is to be terminated; (4) the contract shall include a provision allowing growers to terminate a contract by written notice given 30 days before removal of a flock, and (5) notwithstanding any confidentiality clauses, growers shall be permitted to discuss the offered contract with their financial and business advisors. These

new requirements will improve market transparency and protect growers by providing more information at an earlier stage in the contracting process before they have invested in poultry houses. P&SP received more than 400 comments in response to a Notice of Proposed Rulemaking published on August 1, 2007.

Clarify Weighing Regulations

Concern: Several current regulations contain redundancies and inconsistencies, or are otherwise unclear. These include:

- Section 201.49 (9 CFR Part 201)—Requirements regarding scale tickets evidencing weighing of livestock, live poultry, and feed,
- Section 201.76 (9 CFR Part 201)—Reweighing,
- Section 201.82 (9 CFR Part 201)—Care and promptness in weighing and handling livestock and live poultry, and
- Section 201.108–1 (9 CFR Part 201)—Instructions for weighing live poultry.

Violations of these sections of the regulations are deemed to be unfair or deceptive practices and to constitute violations of Section 202 (7 U.S.C. 192) or Section 312 (7 U.S.C. 213) of the P&S Act. Packers and swine contractors may be assessed civil penalties of up to \$11,000 (7 U.S.C. 193) for each violation of Section 202. Market agencies and dealers may be assessed civil penalties of as much as \$11,000 (7 U.S.C. 213) for each violation of Section 312. Given the consequences for violating these regulations, it is important that these regulations be clear.

Additionally, the practices of delaying the weighing of livestock and poultry; loading poultry from multiple growers into one trailer load; failing to use scales correctly; and failing to accurately weigh unused feed at the time it is collected could result in incorrect settlement payments to poultry and livestock growers.

P&SP Action: P&SP proposes to amend Sections 201.76, 201.82, and 201.108–1 to include provisions regarding the weighing of feed. The proposed amendments will ensure that the weighing process is fair and accurate for all growers. P&SP proposes that feed for each grower be weighed on a certified scale, and that a scale ticket be generated at the time the feed is picked up from each grower, before proceeding to another grower to pick up unused feed. P&SP also proposes new requirements for the correct

use of on-board weighing systems to ensure that unused feed is weighed accurately at the time of pickup, although P&SP is not requiring that on-board weighing systems be used. P&SP published a Notice of Proposed Rulemaking on February 11, 2008.

Use of Actual Weights in Livestock, Poultry, and Feed Weighing

Concern: A failure to use actual weights of livestock, poultry, and feed to determine payment represents an unfair and potentially unjustly discriminatory practice in violation of the Act. This practice could result in a livestock or poultry grower receiving less than full payment for his/her production.

P&SP Action: P&SP is considering amending Section 201.55 of the regulations to require that, for the purchase, sale, and acquisition of livestock, poultry, and feed, the actual weight shown on a scale ticket must be used to determine payment or settlement. P&SP also proposes to remove current language allowing for the use of “reasonably determined” estimated weight rather than actual weight. P&SP is developing a Notice of Proposed Rulemaking for publication in the Federal Register.

REPORT PROVENANCE

Congress mandated specific content of this Packers and Stockyards Program 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)

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