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

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Agricultural Supply Management Programs

- **Private**, industry funded and administered **programs**
  - No government involvement
- The **organizations of agricultural producers** (cooperatives, associations, etc.) develop and implement these programs
  - Participation of agricultural producers is voluntarily
- The **scope** of possible activities is **broad**
  - “Supply” may refer to **agricultural output** at the **pre-production, production** and **post-production** (marketing) stages of the supply chain
- Markets affected: **dairy, potatoes, eggs**
- **Common features** of agricultural supply management programs
  - **Objective:** To achieve a **fair level of returns** for agricultural producers and **to stabilize prices** received by producers
  - **Design:** Some form of **production restrictions** and some form of **post-production supply management**
Legal Foundation: Capper-Volstead Act (1922)

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

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

Triangle ABC is a deadweight loss due to monopoly market power. Rectangle PpcPmAB is a monopoly overcharge. Trapezoid PpcPmAC is a reduction in the consumer surplus due to monopoly power.
Supply Management in Dairy and Potato Industries

- **Economic forces** leading to the decision on supply management
  - Over-supply of milk and potatoes, increasing output price volatility and increasing level and volatility of agricultural input prices
  - Decreasing government support and increasing exposure to international markets
  - Financial stress and adverse effects on the profitability of farmers

- **Dairy**: Cooperatives Working Together (2003-2010)
  - *Herd retirement program* was used to remove from production the entire milking herds of selected dairy farmers
  - *Dairy export assistance program* provided subsidies on export of butter and cheese

- **Potatoes**: United Potato Growers of America, United Fresh Potato Growers of Idaho and other regional cooperatives (2005-2010)
  - *Potato acreage management program* was used to control the number of potato acres planted
  - *Marketing programs* included potato flow control, exchange of marketing information and secondary marketing strategies diverting excess supply of already produced potatoes
• There is **evidence** on milk and potato **supply reduction**
• Key Question: Was the supply reduction reflected in **a higher price**?
• According to empirical findings reported in the literature
  • **The milk price increase ranges** (vary with demand elasticity)
    • Parkinson (2008): $0.28/cwt to $0.51/cwt
    • Brown (2009): $0.22/cwt to $1.54/cwt
    • McCay (2011): $0.21/cwt to $0.62/cwt
    • “Reference” price: $13.67/cwt
  • **The potato price increase ranges**
    • Bolotova et al (2008): $2.41/cwt - $2.74/cwt
    • Bolotova (2008): $0.61/cwt
    • “Reference” prices: $3.89/cwt; $4.93/cwt; $7.78/cwt
• Results to be interpreted with caution
  • Different methodologies, data sources, data frequency, analyzed time periods and regions, empirical procedures, model specifications
  • Whether the **production cost increases** were taken into account
  • Relative to which *reference price* the price increase was calculated
**Antitrust Issues: Current/Recent Private Lawsuits**

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

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

• A common perception among industry participants is that Capper-Volstead Act protects supply management activities, including production restrictions
  • In light of economic theory, the market effect of output control is similar to price-fixing, which is immune based on case law
  • A number of industries openly implemented supply management programs for several years
  • Alternative: Marketing Orders/Agreements would require federal government participation -> much more complex process and issues with WTO domestic support limits

• In Re: Fresh and Process Potatoes Antitrust Litigation (12-2011)
  • The first in Capper-Volstead Act history interpretation of legal status of supply management practices
  • Court “Advisory Opinion”: “Acreage reductions, production restrictions, and collusive crop planning are not activities protected by the Capper-Volstead Act”

• The antitrust enforcement agencies, Department of Justice and Federal Trade Commission, rely on case law in their antitrust enforcement efforts
Antitrust Issues: Legal Uncertainty

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

**Concerns of antitrust authorities**

• The market effects of collective actions of agricultural producers
  • Higher prices for buyers and final consumers, quantity reduction, and deadweight loss

• Agricultural cooperatives are compared to classic cartels (typically operate in oligopolistic markets = “a few” market players)
  • Presumption: they have large market shares and therefore possess market power, which allows to use output control to increase price

**Response**

• Ag markets - perfectly competitive environment ("many" ag producers)
• A large membership of agricultural cooperatives and uncertainty of agricultural production make agricultural output control more difficult to implement
  -> it is more challenging to achieve a sustainable price increase
• Over-supply problem: Output prices are below production costs
Agricultural supply management is a measure that effectively allows to deal with a number of economic forces adversely affecting modern agricultural production:

- Increasing input and output price volatility, over-supply problem, low return level, middlemen market power

Should be aware of legal challenges:

- During legal proceedings, supply management practices are interpreted on a case-by-case basis
  - What is “legal” for one industry may be “illegal” for another one
  - It is important to distinguish between pre-production, production and post-production supply management
  - The latter is more likely to be interpreted as “marketing activities” protected by Capper-Volstead Act

Should be thinking about alternative practices/programs:

- Various forms of price control
  - “Price-fixing” has been interpreted as an element of “marketing activities” generally protected by Capper-Volstead Act
  - “Public” programs – involve government participation
Questions ???

Comments ...

Thank You

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