

## The Open Markets Institute's Comments on USDA's Proposed Rule on Transparency in Poultry Grower Contracting and Tournaments

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Washington, DC 20250-0201

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Via Online Submission

Dear Mr. Offutt:

The Open Markets Institute\* welcomes the opportunity to offer its perspective on the United States Department of Agriculture's (USDA) proposed rule to increase transparency in poultry contracting and tournament systems under the Packers and Stockyards Act (PSA).

The Packers and Stockyards Act is a critical statute passed a century ago to establish fair conduct in the livestock industry. Congress passed the Act after an investigation by the Federal Trade Commission (FTC) found that a few meatpacking corporations abused their monopolistic market power to harm farmers, competitors, and consumers. Congress clearly intended for the Packers and Stockyards Act to have a broad jurisdiction that went beyond previous antitrust laws to prevent monopolistic, unfair, deceptive, and otherwise abusive conduct by meatpackers.<sup>1</sup>

Unfortunately, the meatpacking industry today is more concentrated than it was at the time that the PSA was passed; and recent price- and wage-fixing allegations suggest that packers once again exert immense power to manipulate markets.

Such consolidation harms consumers, workers, and farmers. One lawsuit estimates that alleged collusion among chicken processing companies cost the average family of four an extra \$330 on chicken per year in the late 2010s.<sup>2</sup> Wage-fixing allegedly stole competitive wages from the largely immigrant poultry-processing workforce.<sup>3</sup> Meatpacker consolidation has also decreased,

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\* The Open Markets Institute is a nonprofit organization dedicated to promoting fair and competitive markets. It does not accept any funding or donations from for-profit corporations. Its mission is to safeguard our political economy from concentrations of private power that undermine competition and threaten liberty, democracy, and prosperity. The Open Markets Institute regularly provides expertise on antitrust law and competition policy to Congress, journalists, and other members of the public.

<sup>1</sup> See 61 CONG. REC. 1806 (1921). (During debate on the Packers and Stockyards Act, Rep. Samuel Rayburn said about the PSA that “[Congress] gave the Federal Trade Commission wide powers, but not as wide as they give the Secretary of Agriculture under this bill”).

<sup>2</sup> Ben Popken, *You're Getting Skinned on Chicken Prices, Suit Says*, NBC NEWS, (Feb. 17, 2017), <https://www.nbcnews.com/business/consumer/you-re-getting-skinned-chicken-prices-suit-says-n721821>.

<sup>3</sup> Complaint at 17-49, *U.S. v. Cargill, et. al.*, No. 1:22-cv-01821-ELH (D. Md. filed Jul. 25, 2022).

and in some cases, eliminated, competitive bidding for livestock, suppressing the prices farmers are paid for their animals.<sup>4</sup>

USDA's proposed rule addresses one facet of unfair dealing in the meat industry: information asymmetries between contract chicken growers and poultry dealers. The vast majority of U.S. chickens are raised by contract growers on behalf of chicken processing companies (herein poultry "dealers" or "integrators"). Chicken dealers have vertically integrated most steps of the chicken supply chain and control the supply of chicks, feed, veterinary services, and other inputs provided to contract growers. Integrators also specify what type of facilities contract growers need to raise the birds in. Contract growers are responsible for building and maintaining these chicken houses and tending flocks as they grow. Dealers pick up fattened birds and pay contract growers based on the final weight of their flock. Most dealers pay farmers through an unfair tournament payment system, which ranks growers' performance against others in their region, giving high-ranking growers a bonus and deducting from the base pay of low-ranking growers. Because integrators have unaudited control over the inputs that determine farmers' ranking, integrators can arbitrarily influence farmers' income.

Under this rigged system, poultry dealers possess more information than contract growers about the pay variation among them and about the differences in the quality of key inputs provided to them. Without this information, farmers risk signing growing contracts that lock them into substantial debt obligations and variable income. Farmers also lack audited information about the quality of their inputs and the quality of inputs given to other farmers whose performance they are ranked against in tournament payment systems. Without carefully audited information, farmers cannot know if their performance and tournament system ranking is related to their management decisions or differences in inputs provided by poultry dealers.

USDA's proposed disclosures would require poultry dealers to share the full range of incomes that growers in a given region could possibly receive, as well as more information about the inputs that each grower in a tournament payment pool received. Having this information may change bargaining dynamics in the chicken industry by allowing farmers to make more informed business decisions and avoid signing misleading or deceptive contracts. These disclosures will also help farmers identify trends of mistreatment or undue preferencing, such as an inequitable distribution of poor-quality inputs.

However, these disclosures alone will not be sufficient to address the fundamental power imbalances between contract growers and poultry integrators, which USDA recognizes in their proposal. So long as chicken farmers cannot meaningfully negotiate contracts with poultry companies, disclosures will not necessarily prevent companies from offering take-it-or-leave-it contracts or using unfair payment systems, such as the tournament system, to manipulate and exploit farmers.

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<sup>4</sup> See James M. MacDonald and Nigel Key, *Market Power in Poultry Contracting? Evidence from a Farm Survey*, 477-490, 488 (Journal of Agriculture and Applied Economics, 2012). ("... growers facing a single integrator are paid 7-8% less, on average, than farmers located facing four or more integrators."). See also FRANCISCO GARRIDO ET AL., RANCHERS-CATTLEMAN ACTION LEGAL FUND UNITED STOCKGROWERS OF AM., BUYER POWER IN THE BEEF PACKING INDUSTRY: AN UPDATE ON RESEARCH IN PROGRESS 24 (Mar. 30, 2022) <https://www.r-calfusa.com/wp-content/uploads/2022/03/220331-cattlemarkets.pdf>

Many chicken companies exert monopsonist control over growers. A 2014 study by USDA found that half of all poultry farmers reported having just one or two poultry dealers with whom to contract in their region.<sup>5</sup> Due to regional market concentration, integrators may not offer sufficient incentives to compete for farmers' business and farmers may have little choice but to accept unfair contracts even when their risks or deficiencies are adequately disclosed. Poultry integrators exert additional monopsonist control over growers once they have signed contracts due to switching costs, such as company-specific barn upgrades, that prevent growers from easily switching between competing poultry dealers. One recent lawsuit even alleges that poultry dealers maintain no-poach conspiracies to avoid competing for each other's growers.<sup>6</sup>

Requiring additional disclosures without addressing consolidated market power or restricting the use of unfair business practices can have perverse outcomes. Take the example of franchising. The USDA references the FTC's franchising disclosure rule (16 C.F.R Part 436) as a model for its proposal. This rule requires the corporations that control franchises to provide more information to prospective franchisees so that they can adequately weigh the risks and benefits of entering into a franchise agreement. Franchising agreements include similar power dynamics and vertical restraints as poultry contracts. Franchisors can dictate business terms that limit the autonomy of franchisees like setting menu pricing, business hours, and vendors. This gives franchisors control over their networks without taking on the legal responsibilities of owning and running their outlets, making franchisees and their workers more vulnerable, much as is also true of integrators and poultry growers.

Unfortunately, the history of such disclosure rules in franchising is mixed at best. As franchising grew in the 1970s, franchisees challenged restrictive franchising terms, prompting state lawmakers and federal regulators to consider various methods to regulate franchising, including banning unfair methods of competition in the industry. Industry trade groups (predominantly the International Franchise Association) opposed most regulations and pushed for pre-contract disclosure laws instead, which the FTC eventually implemented.<sup>7</sup> The FTC's disclosure rule did not challenge franchisors' vertical restraints, but it did require franchisors to disclose more information about the cost of the business, the franchisor's bankruptcy history, their fee structure, and the franchisee's obligations, among other things.

Since the FTC's disclosure rule, franchisees have not gained much, if any, additional leverage in negotiating agreements with franchisors. In some cases, the rules undermined franchisees. One effect of this rule has been to endorse deceptive and unfair practices within the franchising

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<sup>5</sup> See James M. Macdonald, *Technology, Organization, and Financial Performance in U.S. Broiler Production*, EIB-126, U.S.D.A. ERS, (June 2014) <https://www.ers.usda.gov/publications/pub-details/?pubid=43872>.

<sup>6</sup> Seth Bodine, *Tyson, Perdue Farms Shell Out \$36 Million to Settle Antitrust Claims*, HARVEST PUBLIC MEDIA, (September 1, 2021), <https://www.tspr.org/harvest-public-media/2021-09-02/tyson-perdue-farms-shell-out-36-million-to-settle-antitrust-claims>.

<sup>7</sup> Brian Callaci, *Control without responsibility: The legal creation of franchising 1960-1980* 1-27, 19 (Washington Ctr. for Equitable Growth, Working Paper, 2018), <https://equitablegrowth.org/wp-content/uploads/2018/12/1213-callaci.pdf>.

industry, so long as they are disclosed.<sup>8</sup> Because franchisors can say that they complied with all disclosures, franchisees have less legal standing to challenge unfair franchising agreements as unconscionable.<sup>9</sup>

To be sure, the USDA's proposed rule provides some key benefits to farmers that the FTC's franchising rule does not, such as requiring poultry companies to disclose farmers' minimum potential revenue stream through a commitment to a minimum number of flock placements at a certain flock density. It will also increase the Packers and Stockyards Act's enforcement by creating a clear paper trail of potential undue preferences or input quality discrimination between farmers, provided adequate auditing and information integrity. But the history of the FTC franchising rule suggests that disclosure alone is an imperfect solution to corporate domination and unfair business tactics.

For these reasons, USDA must consider additional rulemakings that prevent chicken companies from using certain payment, contracting, and marketing practices that are unfair, deceptive, monopolistic, or that abuse their dominance to further control the market. The Open Markets Institute is encouraged to see the USDA consider such action in its advanced notice of proposed rulemaking regarding tournament payment systems, specifically.

Tournament payment systems determine farmers' pay based on differences in inputs such as feed, bird health, flock density, and pick-up timing that are controlled by poultry dealers. It is not fair to set farmers' pay based on factors beyond their control. It is also not fair to pay farmers based on their relative performance to a variable average. In tournament systems, farmers that might perform above average nationally can still get penalized and docked pay if they happened to be placed in a tournament complex with other above average growers or too few growers. The Open Markets Institute looks forward to further sharing our thoughts on tournament system regulation in future comments.

Recognizing the limitations of this proposed rule, the Open Markets Institute nonetheless acknowledges that it would be a step forward for increased transparency and more honest contracting in the poultry industry. The rule would provide growers with critical information to help them better assess the risks of poultry contracting. It would also allow farmers to make more informed management decisions and allow them to identify any unfair treatment or favoritism by poultry dealers. This increased transparency and reduced information asymmetry could somewhat redress the imbalance of power between poultry dealers and contract growers, marginally improving the fairness of competition for growers' services. Because this rule would support poultry growers more than it may hurt them, the Open Markets Institute supports this proposed rule. This comment will elaborate on the benefits of USDA's proposed rule and suggest some additions to strengthen the rule.

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<sup>8</sup> *Id.* at 21. ("Franchisee lawyer and head of the American Association of Franchised Dealers Robert Purvin argued during the FTC's 1995 review that the rule 'has achieved a situation of legitimizing what I call systematic fraud.' As franchisee attorney Harold Brown remarked, 'with the adoption of this rule in 1979, the FTC has, for almost all practical purposes, withdrawn from the conduct regulation activity in which it previously was occupied.'").

<sup>9</sup> *Id.* at 21.

## Proposed Rules Address Information Asymmetries for Fairer Contracts

It has been well documented that the current lack of information available to poultry farmers puts them at a greater disadvantage when negotiating or renegotiating contracts with poultry dealers.<sup>10</sup> Growers may decide to invest in costly poultry houses based on misleading income projections or promises. Having more information about expected costs, expected number of flocks, and a range of possible incomes, will help growers make stronger business decisions and better understand their arrangements with poultry integrators.

One of the most egregious information asymmetries that currently exists in the poultry industry is the extent to which farmers' pay may vary under the tournament payment system. Even if there are small performance differences between growers in a pool, the lowest ranked will receive substantial deductions in pay. By one grower's estimate, bottom-ranking growers may receive half as much for their flocks as the median or average grower. Prospective growers presented with pay averages or rosier pay projections may not be aware of this risk when deciding to sign a growing contract.

USDA's rule would require poultry dealers to provide a more honest projection of growers' potential pay variance when signing a contract. By requiring that dealers disclose the average pay of growers in a given region, broken up into quintiles, prospective contract growers will clearly see what the top 20% and bottom 20% of farmers in their region are making with that integrator and can assess their income variation risks accordingly.

The proposed rule would also require that poultry dealers guarantee an annual minimum number of flock placements and a minimum flock stocking density to improve transparency and income predictability for farmers. Farmers are paid based on the weight of their flocks, thus guaranteeing a minimum number of flocks with a certain number of birds can provide some annual revenue assurance. Currently, farmers may budget to raise a certain number of birds per year and receive fewer or smaller flocks from integrators, decreasing their overall revenue. Proper disclosures of stocking density and flock placement minimums will ensure far more accurate and predictable income projections.

That said, committing to a minimum flock and stocking guarantee does not eliminate the chance that integrators engage in other deceptive or unfair practices that result in lower-than-expected incomes for farmers. Farmers do not control many key inputs such as feed, bird health, and bird pick-up, that determine their performance rankings. Thus, USDA's proposed rule would require that a poultry integrator disclose that the integrator has "full discretion and control" over flock placement, flock density, and "other factors" that may affect farmers' income.

It would also require poultry dealers to include information about input quality and variability in their payment settlement sheets given to growers. Per current rules, poultry integrators are required to provide growers with a settlement sheet explaining their final payment, including the number of birds the integrator accepted, the grower's average bird weight, and their payment per

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<sup>10</sup> Leah Douglas & Christopher Leonard, *Is the US Chicken Industry Cheating its Farmers?*, THE GUARDIAN, (Aug. 3, 2019), <https://www.theguardian.com/environment/2019/aug/03/is-the-us-chicken-industry-cheating-its-farmers>.

pound. For growers paid through a tournament ranking system, the settlement sheet also shows where the grower placed in the tournament for that payment period. USDA's proposed rule would expand on these settlement sheet disclosures to include more meaningful information about the differences between growers in a tournament pool.

Under the current requirements, growers do not necessarily know what factors may have contributed to their tournament ranking. Variations in stocking density, veterinary care, feed distribution, chick quality, and other key inputs can all affect the measures that determine growers' tournament system ranking. Under USDA's proposed rule, tournament ranking settlement sheets would need to include more information on these integrator-controlled differences between all the farmers in a pool, as well as information on each farm's chicken housing specifications. For example, in their final flock payment and tournament ranking, growers would be able to see which, if any, factors correlate with higher rankers: perhaps higher-ranked farms received denser flocks, had fewer feed disruptions, or built newer chicken houses. Farms would be assigned some sort of identifier to anonymize the information while allowing farmers to track patterns of top performance or potential preferential treatment over time.

The Open Markets Institute believes that these disclosures will help farmers identify trends in top-ranking farms that could help them make more informed business decisions. They could also help identify differences in treatment or discrimination between farmers to better bring cases of undue preference by packers under the Packers and Stockyards Act. For instance, a poultry grower would be able to see if they are consistently receiving lower quality birds than others or experiencing more feed disruptions.

However, effectively interpreting new settlement sheet disclosures requires honest and accurate information from poultry integrators and growers. USDA's proposal to include auditing requirements for this information is absolutely essential, given ongoing allegations of illegal activity and market manipulation in the poultry industry. But USDA's final rule should include more details on this auditing process to ensure accurate information, especially in settlement sheet disclosures. The rule should specify the minimum qualifications for an approved auditor and the minimum frequency of audits.

Should growers find evidence of inaccurate disclosures, USDA also needs to strengthen PSA prohibitions on deception to ensure farmers can seek justice. The USDA has long held that plaintiffs do not need to prove harm to competition in order to challenge meatpackers under sections 202 (a) and (b) of the Packers and Stockyards Act, which includes a prohibition on deceptive practices. However, several court decisions have incorrectly read a harm to competition standard into sections 202 (a) and (b) of the PSA, hindering farmers' ability to bring deception claims. The USDA should affirm its interpretation through rulemaking.

Further, USDA acknowledges that several of the key variables that affect growers' tournament ranking are determined by poultry integrators. Disclosure of these differences in grower-controlled inputs does not change that. Thus, poultry integrators should have to disclose whether or not their tournament ranking systems account for variability in inputs that are beyond growers' control. This way, growers will be aware if their pay will be substantially determined by variables beyond their control or not. In future regulations, the USDA should consider

mandating fair payment systems that do not determine farmers' pay based on factors beyond their control. Should an integrator provide a farmer with less-than-adequate poults, feed, or medicines; or, if deliveries of the described inputs are not provided or provided late, an integrator should be required to mitigate any deductions in pay due to these circumstances. If the grower believes that they have been unduly punished for inputs beyond their control, then they should have access to an appeals process that will allow their payment to be reviewed and amended. Integrators should also be required to maintain an appeals process for growers to report input quality or delivery issues before they result in unfair pay discrepancies. This process should be disclosed upfront in the contract and all appeals and resolutions should also be disclosed on the grower's settlement sheet.

### **Additional Suggestions to Improve USDA's Proposal**

While the proposed additional disclosures suggested by USDA are helpful in balancing the power inequities between integrators and growers, the Open Markets Institute believes that a few additional areas could still be improved upon with more disclosures.

First, in addition to USDA's proposed payment projection disclosures, USDA should require integrators to disclose the maximum possible pay variance in an integrator's tournament formula. Growers should know the lowest possible payment they could receive as well as the highest possible payment; this could be disclosed as a discrete payment per pound or as a percentage of base pay. These maximum and minimum figures, along with flock placement and flock density minimums, will allow growers to calculate the minimum possible cash flow they could possibly receive in order to fully assess the risk of investing in chicken houses.

Furthermore, USDA has determined that information about an integrator's financial health is essential for growers to determine whether the integrator is likely to remain solvent and fulfill their contract. The Open Markets Institute would argue that the financial health and precarity of other growers working with a particular integrator is also relevant to prospective growers. As per § 201.100(c)(2), the Open Markets Institute would like to see poultry dealers include a summary of the average rate of bankruptcies among growers who have worked with that integrator over the past five years, both nationally and in a grower's tournament complex. Similarly, integrators should also be required to disclose the annual percent of contracts that they terminated over the past five years, annually and regionally. An integrator may provide information as to why growers may have filed for bankruptcy or the most common reasons for contract termination. This information is vital for growers to determine their likelihood of failure. We believe that sharing this information may also incentivize integrators to ensure their growers do not go bankrupt or lose their contract, further protecting individual growers.

To enhance flock delivery transparency, integrators should be required to include a means of identifying each individual flock an integrator delivers as well as each breed of poultry an integrator delivers. This information should be available in addition to already required disclosures indicating the breeder and hatchery from which integrators sourced eggs and poults provided to growers. Growers should be able to access this data going back at least 10 years. This is important for two reasons. First, if a diseased or lower quality flock is placed with a grower, they then have access to tracking information required to participate in an appeals

process should they be punished for less-than-average growth. Second, growers can obtain that breeder's flock-breeding records. Integrators should provide access to the historical data for growers to adequately determine whether the breeders' practices negatively impact final grower payment.

Additionally, to increase transparency and accountability into input quality, integrators should make clear that growers have a right to install feed scales on their farms to independently verify the quantity of feed provided by integrators. Growers report retaliation for installing scales on their farms, even though they already have a right to do so. Independently verifying the quantity of feed provided by integrators can be critical for farmers to determine whether they are being fairly ranked in tournament systems, which value farmers' feed-to-weight conversion ratio. If an integrator reports that it provided a grower more feed than it actually did, the grower gets improperly penalized for having a poorer feed-to-weight conversion ratio.

The USDA proposes a new requirement that integrators give prospective growers the Disclosure Document seven (7) days before the contract would go into effect to allow for grower review. While this requirement is an improvement it is not sufficient to allow farmers enough time to discuss the terms of the contract with relevant entities and make a decision. Fourteen (14) days would be a more appropriate time for farmers to be able to fully research and decide whether the terms of their integrator contract are advantageous.

Finally, the Disclosure Document should be available in languages other than English. The latest data from 2017 shows that there were 112,451 Spanish-speaking agricultural producers in the United States<sup>11</sup>, of which 60 percent live in three states: California, New Mexico, and Texas. If not generally available, at the very least, disclosure documents should be available in Spanish in these three states where Spanish-speaking producers are most heavily concentrated. Additionally, Hmong farmers have been expanding their farm operations into poultry production.<sup>12</sup> Disclosure Documents should be provided in languages other than English in areas where non-English speakers are concentrated and in the languages of those speakers.

Even with all the proposed disclosure rules to be adopted by USDA, growers do not have any guarantee that integrators will not mislead them in providing poor flock placements, poult quality, feed and medicine delivery schedules, or other poultry growing inputs over which growers have no control. The Open Markets Institute believes that the best way to prevent deception, unfair practices, and undue preferences in the poultry industry is to ban the tournament system altogether. We thank the USDA for working to correct information asymmetry by proposing these Disclosure Document rules and we look forward to seeing even more stringent rulemaking to correct poultry tournament compensation system power imbalances in the future.

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<sup>11</sup> NSS, ACH17-10, *2017 Census of Agriculture Highlights: Hispanic Producers*, U.S.D.A. (Oct. 2019), [https://www.nass.usda.gov/Publications/Highlights/2019/2017Census\\_Hispanic\\_Producers.pdf](https://www.nass.usda.gov/Publications/Highlights/2019/2017Census_Hispanic_Producers.pdf).

<sup>12</sup> Chao Xiong, *Hmong Are Moving Again, This Time to Poultry Farms*, WALL ST. J., (Jan. 26, 2004), <https://www.wsj.com/articles/SB107508055242111254>.