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PACKERS AND STOCKYARDS PROGRAMS

Continuing Problems with GIPSA Investigations of Competitive Practices

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G A O

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Mr. Chairman and Members of the Committee:

I am pleased to be here today to discuss the U.S. Department of Agriculture's (USDA) management and oversight of the Packers and Stockyards Act. Within USDA, the Grain Inspection, Packers and Stockyards Administration (GIPSA) is responsible for administering the Packers and Stockyards Act and investigating concerns about unfair and anticompetitive practices in the \$90 billion livestock market.

As you know, prior reports issued by the USDA Office of Inspector General (OIG) and our office have identified weaknesses in GIPSA's investigation and enforcement activities, and recommended actions to address them.¹ A more recent OIG report shows that, in several key areas, GIPSA still has not taken sufficient steps to address those recommendations.² My testimony today will focus on our prior work and discuss (1) factors that have affected GIPSA's ability to investigate concerns about anticompetitive practices, (2) GIPSA's actions to address our recommendations and areas where their efforts have fallen short, and (3) challenges and other issues we believe GIPSA should consider as it moves to further strengthen its capacity to address competitiveness issues.

In summary, in 2000, we identified two critical factors that detracted from GIPSA's ability to investigate anticompetitive practices in livestock markets, and another area where improvement was needed. First, the agency's investigations were planned and conducted primarily by economists without the formal involvement of attorneys from USDA's Office of General Counsel (OGC). As a result, a legal perspective that focused on assessing potential violations was generally absent when investigations were initiated and conducted. Second, GIPSA's investigative practices were designed for traditional trade practices and financial issues the agency had emphasized for years and were not suited for the more complex competition-related concerns it was addressing. Finally, while not a critical concern, we noted that GIPSA had an

¹U.S. Department of Agriculture, Office of Inspector General, *Agency Efforts to Monitor and Investigate Anti-competitive Practices in the Meatpacking Industry*, Report No. 30801-01-Ch (Washington, D.C.: February 26, 1997) and GAO, *Packers and Stockyards Programs: Actions Needed to Improve Investigations of Competitive Practices* (Washington, D.C.: September 21, 2000).

²U.S. Department of Agriculture, Office of Inspector General, *Grain Inspection, Packers and Stockyards Administration's Management and Oversight of the Packers and Stockyards Programs*, Report No. 30601-01-Hy (Washington, D.C.: January 10, 2006).

important role in keeping the industry and the Congress informed about its monitoring of livestock markets and could have done more to identify market operations or activities that appeared to raise concerns under the Packers and Stockyards Act. In our September 2000 report, we recommended that USDA better integrate attorneys from USDA's Office of General Counsel into GIPSA's investigative processes and develop a teamwork approach to investigations similar to that of the Department of Justice (DOJ) and the Federal Trade Commission (FTC). We also recommended that GIPSA adopt more systematic approaches for selecting cases and conducting investigations.

USDA concurred with our findings and noted specific actions it planned to take in response to our recommendations, including (1) formalizing consultations between GIPSA and OGC on complex investigations, and integrating OGC attorneys into its investigative teams; (2) developing a tiered process whereby routine investigations would be reviewed and approved by headquarters staff, while complex investigations received an additional OGC review; (3) adopting relevant procedures used by DOJ and FTC for planning, developing, implementing, and reviewing investigations; and (4) reporting publicly on changing business practices and activities that raise fairness and competition concerns. Despite these plans, the January 2006 OIG report identified substantial ongoing weaknesses in GIPSA's investigative processes and noted that GIPSA's actions to respond to the prior OIG and GAO reports had fallen short in key areas. In particular, GIPSA had not yet developed a teamwork approach for investigations whereby GIPSA's economists and USDA's OGC attorneys could work together to identify violations of law, nor had it taken sufficient steps to ensure legal specialists within GIPSA were used most effectively. In addition, GIPSA had not followed through in adopting appropriate investigative guidance similar to those of DOJ and FTC to strengthen its ability to investigate anticompetitive and unfair practices.

Given GIPSA's lack of progress in addressing prior report findings and recommendations dating back for almost a decade, continued vigilance and monitoring of its key activities and management initiatives by the OIG and other oversight bodies is essential. In its response to the OIG's 2006 report, GIPSA noted that it intends to reassess and develop a defined process for managing investigations, enhancing communication among staff and managers, appropriately dividing responsibility for its varied types of investigations, and developing an internal review function to monitor and report on corrective actions resulting from the OIG and GAO reviews. Consistent with our prior recommendations, GIPSA also plans to define the role of OGC attorneys and GIPSA legal specialists in investigations and to move forward in identifying and adopting certain

techniques used by the DOJ and the FTC. As GIPSA moves ahead in reexamining its processes it should consider assigning lead roles to OGC attorneys for certain investigations involving complex anticompetitive practices. Finally, going forward, GIPSA's efforts to periodically inform the industry and the Congress about competitive conditions could be of further usefulness. GIPSA plans to complete a study on livestock and red meat marketing practices later this year. While potentially informative to the industry and policymakers, it could also help GIPSA identify current and emerging areas of vulnerability and better target its oversight resources.

Background

The Packers and Stockyards Act was passed in 1921 in response to concerns that, among other things, the marketing of livestock presented special problems that could not be adequately addressed by existing antitrust laws. The provisions of the act were based, in part, on prior antitrust statutes including the Sherman Act and the Federal Trade Commission Act. The Packers and Stockyards Act prohibits packers from engaging in or using any unfair, unjustly discriminatory, or deceptive practice or device, or making or giving any undue or unreasonable preference or advantage to another party. The act also makes unlawful packer anticompetitive practices that are antitrust-type actions, including a packer's activities that manipulate or control prices or restrain trade.

Within USDA, GIPSA is responsible for implementing the Packers and Stockyards Act. GIPSA initiates investigations and actions to halt unfair and anticompetitive practices by meatpacking companies and by other parties involved in livestock marketing. To prove that such an activity has occurred under the act, GIPSA, in most instances, must show that the purpose of the packer's action or its actual effect was to carry out the prohibited activity. GIPSA may also choose to treat such activity as an unfair practice, which may be easier to prove than a violation of the act's antitrust-type provisions. Also, while mergers are a concern because they can reduce competition, the act does not provide USDA with premerger review authority. OGC also has an enforcement role and, among other activities, represents USDA in administrative and court proceedings addressing violations of the act.

The Packers and Stockyards Act allows GIPSA to start investigations and administrative actions to halt packer practices that it deems to be unfair or anticompetitive. When an investigation finds and develops evidence to show that a packer may have engaged in an anticompetitive or unfair practice, GIPSA may file a complaint against the packer. The packer has a right to a hearing, which is held before a USDA administrative law judge.

If, after reviewing the evidence presented by GIPSA and the packer, the administrative law judge decides that there has been a violation of the act, a cease and desist order may be issued, and a civil fine may be levied. An administrative law judge's decision can be appealed to USDA's Judicial Officer, who acts on behalf of the Secretary of Agriculture. The packer, but not USDA, may file a further appeal to a Federal Circuit Court of Appeals.

In 1996, GIPSA reported that dynamic changes had taken place in the cattle and hog industries, including increasing concentration and vertical integration—where packers own the animals. GIPSA stated that these changes had reduced the role of the public markets, where terms of a trade are visible to all. That same year, an advisory committee to the Secretary of Agriculture reviewed the concerns of producers and others about changes in livestock markets and recommended, among other things, a review of GIPSA's efforts to enforce the Packers and Stockyards Act. The Secretary then asked the OIG to review GIPSA's program.

The subsequent OIG report noted that while GIPSA had a credible record in certain areas, it (1) did not have the capability to perform effective anticompetitive practice investigations and (2) faced formidable obstacles to become effective in performing such investigations. The OIG found that GIPSA had not been organized, operated, or staffed for that purpose and stated that GIPSA should employ an approach similar to that used by DOJ and FTC, and integrate attorneys and economists from the beginning of the investigative process. In response, GIPSA completed a major restructuring of its headquarters and field offices in 1999 and hired staff to strengthen its investigations of alleged anticompetitive practices. GIPSA now has regional offices in Denver, Colorado, for its work on the cattle industry; in Des Moines, Iowa, for handling work on the hog industry; and in Atlanta, Georgia, for its work on the poultry industry. Along with those changes there were relocations of staff and the addition of economists and legal specialists to assist with investigations of competitive practices.

Because of continued concerns about whether GIPSA was taking sufficient action to protect competition in livestock markets, GAO was requested to review USDA's efforts to implement the Packers and Stockyards Act. We issued our final report and recommendations for improvement in September 2000. Subsequently, the OIG completed a follow-up review on GIPSA's administration and oversight of the Packers and Stockyards Programs in January 2006. It too issued a report with recommendations.

2000 GAO Review Identified Critical Factors Detracting From GIPSA's Investigative Capabilities

We identified two critical factors that detracted from GIPSA's investigative capability, as well as areas where GIPSA could improve its efforts to develop and share key information. First, the agency's investigations were planned and conducted primarily by economists without the formal involvement of attorneys from OGC. Second, GIPSA's investigative practices were designed for traditional trade practices and financial issues the agency had emphasized for years and were not suited for the more complex competition-related concerns it was addressing. While not of a critical nature, we also found that despite prior dynamic changes in the livestock markets, GIPSA's efforts to periodically update the industry and Congress on competitive conditions and emerging fairness and equity issues were lacking.

Attorney's Participation in Investigations

At the time of our review, OGC attorneys did not usually participate at the start or throughout the agency's investigations. Assignment of OGC attorneys typically occurred after GIPSA performed an investigation and forwarded a developed case file to them for review and action. Thus, the agency's investigations were planned and conducted primarily by economists, most of whom had limited investigative experience. GIPSA relied on OGC attorneys mainly for legal advice, and its OGC reviewed the results of GIPSA's investigations to determine if violations of law might have occurred. In contrast, we noted that DOJ and FTC utilized integrated teams of attorneys and economists to perform investigations of anticompetitive practices. Attorneys were assigned to lead and conduct investigations from the outset so that officials with a legal perspective focused on assessing potential violations of law. Economists were routinely assigned as an integral part of the investigation teams. This approach ensured that a legal perspective was brought to bear on the interpretation of law, development of evidence, and preparation of cases for presentation in administrative and judicial proceedings.

We also reported that OGC officials provided GIPSA with only limited informal assistance which had declined over the years as the number of OGC attorneys assigned to assist GIPSA decreased. In fact, the number of OGC attorneys assigned to GIPSA cases had decreased from eight to five because of budget constraints, according to USDA's General Counsel. These attorneys were also not all assigned full-time to GIPSA's financial, trade practice, and competition cases; some had responsibilities in other USDA areas as well.

We concluded that GIPSA's program needed additional steps to become more effective and efficient in performing investigations and recommended that GIPSA develop a teamwork approach for

investigations with GIPSA's economists and OGC's attorneys working together to identify violations of the law. We also recommended that the Secretary reassess current OGC staffing needs relative to current GIPSA investigations, assign attorneys to lead or participate in more complex investigations, and increase the effectiveness of legal specialists by providing them with leadership opportunities and better supervision.

Processes and Practices For Anticompetitive Practice Investigations

We also found that GIPSA's basic investigative processes and practices were not designed for addressing the complex anticompetitive practices it had begun to encounter in recent years—instead they were designed for the more traditional trade practice and financial issues that the agency had emphasized for years. In comparison, DOJ and FTC had processes and practices specifically designed for guiding investigations of similarly complex competition-related issues.

DOJ and FTC emphasized establishing the theory of each case and the elements necessary to prove the case. At each stage of an investigation, including selecting the case, planning, and conducting the investigation, regular reviews by senior officials-attorneys and economists—focused on developing sound cases. For example, DOJ and FTC required their attorneys, with the assistance of economists, to establish a theory explaining how a company's (or companies') behavior may be a violation of the law. The case theory and evidence were reviewed early on by senior officials, and periodically as the factual underpinnings of the case came into focus. In contrast to DOJ and FTC, GIPSA does not require investigations to be (1) planned and developed on the basis of how a company's actions may have violated the law and (2) periodically reviewed as they progress by senior officials with anticompetitive practice experience.

GIPSA also did not have specific requirements for approving an investigation or an investigation plan. These conditions were reflected in the comments of GIPSA's regional office managers and economists, who said that they often had questions about how to interpret the law and how best to scope and perform investigations. Also, OGC officials told us that anticompetitive practice cases that GIPSA had forwarded often had weaknesses that needed to be addressed before they could determine whether a violation had occurred. Both OGC and GIPSA officials said that OGC's reviews of GIPSA's cases led to disagreements about the interpretation of the act and the sufficiency of evidence. Finally, we found that GIPSA's investigative guidance manual had not been revised since the agency's reorganization and did not contain specific guidance for anticompetitive practice investigations, such as the contents of an

investigative plan, the information needed for approval of an investigation, or the frequency of reviews of the investigations.

Developing and Sharing Information on Competitive Conditions With Key Stakeholders

GIPSA periodically made educational outreach efforts and shared information via its Web site and annual reports. GIPSA also held and participated in numerous town hall meetings and conferences with producers and state and industry officials. Even so, GIPSA officials said they could do more to inform the industry and others on competitive conditions. In fact, at the time of our review, it had been several years since GIPSA had last reported on conditions in livestock markets, despite previous dramatic changes in industry concentration and vertical integration.

GIPSA officials also recognized that it would be helpful if producers had a more current understanding of the Packers and Stockyards Act and how the act applies to market activities. They also agreed that GIPSA could report on market activities and identify those that may raise concerns about fairness and competition, as FTC had done. In our report, we recommended that GIPSA provide industry participants and the Congress with clarifications of GIPSA's views on competitive activities by reporting publicly on changing business practices in the cattle and hog industries and identifying market operations or activities that raised concerns under the Packers and Stockyards Act. GIPSA has published four such assessments from 2000 to 2004.³

GIPSA's Actions To Address GAO's Recommendations Fell Short in Several Areas

USDA's General Counsel and the Under Secretary for Marketing and Regulatory Programs concurred with our recommendations and provided encouraging details about their planned implementation. Among other things, they stated that GIPSA and OGC would formalize their relationship for complex investigations to ensure that all investigative, economic, and legal issues were carefully considered before embarking on complex investigations. As part of that process, they stated that they were examining the procedures of the Antitrust Division of DOJ and the FTC and would adopt relevant portions for investigation planning, development, implementation, and review. They also stated that GIPSA and OGC senior management would review plans for complex investigations to ensure the effective use of investigative resources and

³GIPSA's report for 2004 was issued in April 2005. U.S. Department of Agriculture, Grain Inspection, Packers and Stockyards Administration, *Assessment of Cattle, Hog, and Poultry Industries* (Washington, D.C.: April 2005).

facilitate successful litigation if evidence demonstrates that the Packers and Stockyards Act has been violated.

The General Counsel and Under Secretary also stated that they would increase the integration of OGC attorneys into GIPSA's investigative teams early in the investigative process. They noted that OGC attorneys would work closely with GIPSA's economists, legal specialists, and other technical specialists to ensure that investigative plans had a sound basis and to address critical legal issues throughout the conduct of an investigation. In addition, the effectiveness of legal specialists was also to be enhanced. However, they stated that GIPSA's legal specialists would not act as attorneys for either GIPSA or the Department, but would provide front-line legal advice on investigations. Legal specialists would also be trained by OGC attorneys and consult with them regularly.

It is troubling that these plans, which appeared to be carefully laid out by USDA in late 2000, were never wholly or effectively implemented as noted in the OIG's 2006 follow-up report. Unfortunately, as the report makes clear, GIPSA's senior management review panel became a log jam to the progress of investigations. Investigations were thwarted by management delays in providing policy and investigative guidance and by inaction on on-going investigations when they required management concurrence or direction. Further, GIPSA and OGC apparently have not effectively implemented a team approach to the investigation of complex competition related investigations. Overall, it appears that as GIPSA officials responded to the prior OIG and GAO reports, they did so in a manner that prevented, rather than facilitated the desired actions and results.

Challenges and Other Issues Associated With Addressing Longstanding Weaknesses

Given GIPSA's lack of progress in addressing prior report findings and recommendations dating back almost a decade, continued vigilance and monitoring of its key activities and management initiatives by the OIG and other oversight bodies is essential.

In response to the most recent OIG report GIPSA has stated that, among other things, it is:

- developing a defined process for managing investigations, including controls for preliminary investigations to obtain sufficient facts to decide whether to proceed with further investigation;
- revising its organizational structure to appropriately divide management responsibility for work plans, managing investigations, and the reporting of results;

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- developing an internal review function to monitor and report on the progress of corrective actions resulting from external reviewers, such as the OIG and GAO;
 - moving forward in identifying techniques used by DOJ and FTC that are most appropriate under the Packers and Stockyards Act.

GIPSA also stated that it will enable its legal specialists to consult with OGC and will integrate attorneys into complex competition investigations earlier in the process.

Beyond increased monitoring, GIPSA's success in fully implementing the above initiatives will require sustained management attention and commitment that has, thus far, been elusive. However, we continue to believe that such a focus is needed and will ultimately result in a more vigilant and skillful federal presence. It will also instill greater public confidence that concerns about the industry will be investigated fairly and diligently. Finally, as GIPSA moves forward in developing its processes, it should consider the feasibility of assigning lead roles to OGC attorneys for investigations that involve more complex anticompetitive practices—an approach we have recommended that is also consistent with DOJ and FTC practices. Going forward, it is also possible that GIPSA's efforts to periodically inform the industry and the Congress about its monitoring efforts, as well as changing competitive conditions could be of further usefulness. GIPSA has issued reports on the cattle, hog, and poultry industries from 2000 through 2004, and has initiated a broad study on livestock and red meat marketing practices. While informative to the industry and policy makers, such analyses could also be internally valuable to GIPSA as a tool for identifying current and emerging areas of vulnerability and better targeting its oversight resources and activities.

Mr. Chairman, this concludes my formal statement. If you or other Members of the Committee have any questions, I will be pleased to respond to them.

For future questions about this testimony, please contact me at (202) 512-5988. Charles M. Adams made key contributions to this testimony.

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