

November 2004

IFAP STATEMENT ON LEGAL AND INSTITUTIONAL ASPECTS OF INDUSTRIAL CONCENTRATION IN THE AGRI-FOOD SECTOR

INTRODUCTION

The inadequacy of current competition rules is one of the most pressing issues facing farmers across the globe. As evidenced by the sharp decline in the number of family farms in the past decade and the increasing trend toward horizontal and vertical concentration in the agriculture and food sector, independent producers cannot succeed in the absence of protection from unfair, anti-competitive practices.

The loss of family farms and other independently owned businesses is not inevitable. IFAP believes that the accelerated march toward a vertically integrated production system can be turned around with action to enforce and enhance antitrust and competition laws, strengthening of the regulatory system, protection of consumers and revitalization of independently owned businesses and competitive markets.

CHANGES IN THE STRUCTURE OF THE GLOBAL FOOD SYSTEM

The economic structure of the food and agricultural system around the world is undergoing major changes. In particular, three processes are occurring simultaneously.

The first process is “horizontal integration” that refers to the increased market concentration and control by a few firms at any stage of the food system, from the production of seed through the retailing of the final product. One of the basic requirements for a competitive system is that no one company is in a position to dominate the market price. Experience shows that when four companies gain control of at least half of the market share between them, this basic requirement for a competitive market system is violated. This concentration of market power distorts the correct functioning of markets.

The second process involved in restructuring of the food system is “vertical integration”. This is the process in which one, or several, companies acquire a significant amount of control over all stages in the food and agricultural system. Mergers and acquisitions is

one way of achieving this control, but it can also occur by other means, such as joint ventures or long-term agreements. This process is often referred to as the development of a food chain or a seamless system. Companies involved in vertical integration can survive on low rates of return in one stage of the system as long as they receive good returns in other stages of the system (cross subsidisation). Those persons involved in only one stage of the system, like farmers who are only involved at the production stage, face serious economic consequences if profits in that stage fall below costs of production.

The third process is “global dominance” of the food system through vertical and horizontal integration in a host of countries around the world by a very limited number of transnational corporations. A corporation operating internationally can operate at a loss in one or two countries for a period of time as long as it receives good profits in other countries. Domestic companies operating in only one country do not have this flexibility and control, and a loss in their national markets can threaten their survival.

WHERE IS INDUSTRIAL CONCENTRATION MOST PREVALENT?

A survey of IFAP member organisations shows that while industrial concentration is occurring in all sectors of the agri-food chain, it is most prevalent in retailing.

In the USA, it appears that retailing may eventually control the transportation and processing sectors too, because retailers have the most direct connection to consumers.

Concentration within the banking industry has also resulted in decreased access to credit for farmers and other small businesses in rural communities in the USA.

Ownership of seeds and breeding stock

Farmers are particularly interested in the state of industrial concentration in the grain and livestock seedstock sectors and the way in which intellectual property concerning living material can be protected. In this respect, it is important to distinguish between two main ways of protection: the plant breeder's licence and the patent¹. Contrary to the plant breeder's licence, the patent system excludes the farmer's privilege (the right for a farmer to keep seeds for resowing on his farm) as well as the breeder's exception, even if certain conditions are fixed.

The IFAP survey of member organisations shows that the situation varies significantly throughout the world. In **Europe**, farmer cooperatives often provide the grain and livestock seedstock to producers. Where the private commercial sector is dominant, the authorities usually provide a legal framework to ensure that farmers have competitive

¹ The plant breeder's licence grants a temporary exclusive exploitation right but, contrary to a patent, it does not allow the breeder to claim a royalty on a new variety developed on the basis of the genetic material of the protected variety: this is the "breeder's exception" principle that favours biodiversity as it enables all breeders to use all marketed propagating material for breeding purposes. Conversely, it is not allowed to use patent-protected plants (belonging to a variety) without the authorisation of the patent holder and without paying a fee, even for research purposes. Hence, contrary to the plant breeder's licence, the patent system excludes the farmer's privilege as well as the breeder's exception, even if certain conditions are fixed.

access to seeds at a fair price, while recognizing that owners should be remunerated correctly.

In most developing countries, only a minority of farmers buy seed and livestock seedstock from commercial companies. For example, in **Uganda** less than 20 per cent of the grain seed used is provided by seed supply firms and less than 2 percent by livestock seed stockists.

In **Kenya**, since the onset of liberalization in the seed sector, over 40 seed companies have been registered. However, less than 10 companies belong to the seed traders association and they control close to 90 per cent of seed production and marketing. Contrary to farmers' expectations, the prices of seeds have not gone down despite intense competition, but instead have gone up and quality has deteriorated. 80 per cent of the farmers in Kenya are smallholders, and they rely heavily on farm saved seeds

On the retail side generally, Kenya has close to 200 supermarkets and 10 hypermarkets controlling equivalent in sales of 900,000 small shops and accounting for 30% of food retail (FAO 2003). They purchase 3 times more produce from local farmers than Kenya exports to the rest of the world.

Farmers in the **USA** expressed most concern over the small number of entities controlling the grain and livestock seedstock. As vertical integration continues to grow, the control of agribusiness chains over the food and fibre system from “gene to plate” is deepening.

In the case of grain, the same companies that buy the grain own the seed. In many cases, contracts require farmers to plant the seed grain supplied by the companies.

In the case of poultry, nearly all production in the USA is done under contract. The producers own the buildings, but the processors own the birds and provide them to the producers. A 1999 study commissioned by the US National Farmers Union cited the fact that only six breeding stocks of turkeys remain. A similar situation also exists in some European countries.

CONSUMER ORGANISATIONS – do they feel concerned?

Consumer organisations might be expected to share farmers' concerns about industrial concentration in the agri-food sector, since most of the concentration is taking place in retailing. However, consumer organisations seem more interested in food quality assurance schemes than industrial concentration. Only a few of the consumer organisation websites that were searched on the Internet mentioned industrial concentration in the agri-food sector as an issue for them.

Consumer organisations in countries like Denmark and the USA have expressed support for farmers' fight against concentration in the agri-food sector. However, the consumer movement is not leading the charge against agricultural concentration.

Nevertheless, consumer organisations are aware of the difficulties facing small agricultural producers both in the industrial countries but particularly in the global South. They see the cause as “an agribusiness-driven system in which structurally depressed prices for agricultural commodities benefit neither farmers nor consumers”.²

Southern governments, often as part of the conditions of IMF and World Bank adjustment programmes, have abandoned mechanisms for agricultural support and state intervention, despite the global imbalances in agricultural market liberalisation. The withdrawal of credit, input, marketing and technical support for small producers has hindered their ability to respond effectively to domestic and external market opportunities, and, the frequent absence of effective competition regulation has meant that benefits have not necessarily been passed to consumers.

Smaller producers, generally, while often efficient and responsive, are often at a disadvantage in bargaining with the buying and selling power of large national and foreign processing firms and retailers dominating domestic and foreign markets. A global supermarket sector now exists with 30 companies accounting for one third of grocery sales, and supermarket chains are rapidly penetrating the markets and middle- and even lower-income countries.

The consumer implications of the apparent trend towards growing concentration in agrifood markets merit further detailed study, both in terms of the relationship between the welfare of rural and urban consumers in the developing and transition economies and in terms of the links with the interests and responsibilities of consumers in OECD countries. Consumers’ International has indicated that it would welcome the opportunity to explore with farmers’ organisations and other stakeholder groups how and to what extent producers and consumers have common interests in seeing this issue addressed in agricultural reforms and wider efforts to deal with the role of anti-competitive practices.

COMPETITION AUTHORITIES

Competition authorities generally exist throughout the industrialised countries, but are not yet established in most developing countries.

It is extremely important that competition authorities recognise the social benefits gained from the existence of strong farmer co-operatives and do not hinder the structural adaptation that many agricultural co-operatives must undertake if they are to survive in the increasingly competitive international markets and a highly concentration food chain.

² See *Multilateral Disciplines to Phase Out Agricultural Dumping*, <http://www.tacd.org/cgi-bin/db.cgi?page=view&config=admin/docs.cfg&id=199>

USA

In the USA, the United States Department of Justice (DoJ) and the Federal Trade Commission (FTC) have jurisdiction for reviewing mergers and acquisitions involving large firms, under federal antitrust law. The two agencies make joint decisions about which department will handle each case.

The United States Department of Agriculture (USDA) has federal authority over livestock competition issues, under the Packers and Stockyards Act (PSA). In general, the PSA prohibits meatpackers from engaging in or using any unfair, unjustly discriminatory, or deceptive practices or devices in commerce. A recent legislative proposal would have given USDA an advisory role in considering mergers dealing with agricultural firms. However, Congress has not acted on the proposal.

Under United States federal law, firms of a certain size must file statements of intent with the government prior to a merger or acquisition of another firm if the second firm also meets the assets threshold. The merger is allowed to go forward unless the government files a lawsuit to prevent the merger within the time specified by statute.

In addition, there are some state laws dealing with market competition issues in the USA.

European Union

The European Union's system for monitoring merger transaction has been governed by the Merger Regulation (Council Regulation 4064 of 1989) since 1990. The Merger Regulation removes the need for companies to seek clearance for certain large-scale mergers in a myriad of different national regimes and ensures that all such mergers receive equal treatment.

The Merger Regulation gives the European Commission the exclusive power to investigate mergers with a 'Community dimension'. The Merger Regulation defines the 'Community dimension' of a merger or using thresholds based on the turnover of the companies involved. The most important are the worldwide threshold (5,000 million Euros) and the Community-wide threshold (250 million Euros). Below these thresholds, merger control is carried out by the authorities in the Member States under their own national legislation. These thresholds are quite arbitrary as they take no account of the relative size of the market under consideration.

Mergers and acquisitions with an EU-wide, or Community, dimension must be notified to the Commission for its agreement before they are put into effect.

In December 2001, the Commission adopted a Green Paper aimed at launching a debate on the functioning of the European Union's merger control law. After wide-ranging consultations, an extensive reform package was adopted by the Commission in December 2002, together with a proposal for a revision of the Merger Regulation.

A new merger control law was adopted by the Council of Ministers on 20 January 2004, and its application began on 1 May 2004. The regulation was extended to the whole of the European Economic Area on 8 June 2004 by decision of the EEA Joint Committee.

Belgium

Competition policy in individual EU member states is based on European Union legislation. The administration of this policy is translated into national legislation.

In Belgium, the Act of 1 July 1999 assigns responsibility for overseeing competition to four bodies:

- § the Competition service
- § the Corps of rapporteurs
- § the Competition Council
- § the Competition Commission

In addition, the Minister with responsibility for Economic Affairs and the Council of Ministers has a number of competition-related powers.

The “Competition Service”, which is a unit of the Ministry of Economic Affairs, is responsible for seeking out and noting the existence of anti-competitive practices. It investigates all cases in which action must be taken and enforces any rulings.

A “Corps of rapporteurs” has been set up within the Competition Service. Their main tasks are to:

- § head and organise investigations
- § issue instructions to agents assigned to carry out investigative measures
- § prepare investigative reports and submit them to the Competition Council.

The Competition Service and the Corps of rapporteurs assist European competition authorities with enforcement of EU rules on competition.

The Belgian “Competition Council”, set up under the auspices of the Ministry of Economic Affairs, is an administrative entity having the authority to take decisions, put forward proposals and give opinions. Under its decision-making powers, it ascertains whether or not prohibitions of restrictive practices have been infringed, and it alone is empowered to grant individual exemptions at the request of the enterprises involved. It also rules on the acceptability of concentrations.

The Competition Council is made up of 20 members, appointed for a six-year renewable term, some from among judicial magistrates and some by virtue of their expertise in the area of competition. The Chairman, Vice-Chairman and two other members hold full-time positions.

The “Competition Commission” is an advisory body representing the viewpoints of labour, industry, agriculture, commerce, crafts and consumers. Among its functions is to issue opinions, on its own initiative if it so chooses, on any matter involving general competition policy. The farmers’ union, Belgian Boerenbond, is represented in the Competition Commission.

The “Minister responsible for Economic Affairs” can ask the Corps of rapporteurs to carry out investigations and to conduct general or sector-specific investigations. The Minister can also lodge an appeal with the Brussels Court of Appeal contesting the decisions of the Competition Council.

When it is in the public interest, the “Council of Ministers” may authorise, either on its own authority or at the parties’ request, a merger or concentration that the Competition Council found inadmissible.

Uganda

As in most developing countries, competition laws for the agri-food sector are not yet pronounced in Uganda. Otherwise the Cooperative Department, Uganda Investment Authority and the Registrar of Companies are responsible for ensuring that similar processing plants are not established too close together in any single production area.

Kenya

The government is encouraging investors both domestic and external to take advantage of the enabling environment and invest more especially in the agriculture sector.

GOVERNMENT ACTION AGAINST INDUSTRIAL CONCENTRATION

Few governments seem to be actively pursuing means to slow, stop or reverse the trend of industrial concentration in agriculture or food industries.

In **Belgium**, the government is working hard on concentration issues in for example the pharmaceutical sector. In the **USA**, government has taken action in two notable recent lawsuits to require some divestiture by Microsoft (computers), and to prevent an acquisition of Direct TV by Echostar (telecommunications). However, the government has been less restrictive in agricultural acquisitions and mergers.

At the farm level, some **European** governments are promoting differentiation, regional marketing and niche-productions. However, while this may be a solution for some farmers, the majority of production will still move through the large established supply chains. The main solution is therefore for farmers to collaborate either horizontally or vertically to obtain a greater share of the value chain.

RECOURSE OPEN TO FARMERS WHEN HARMED BY CONCENTRATION – possibility of class actions

In the IFAP survey of member organisations, farmers from several countries said that legal or civil remedies are available to farmers who have been harmed by concentration.

In **Denmark**, farmers can make complaints to the Danish Competition Authority. The Danish Farmers’ Union has done this on behalf of farmers on several occasions.

In **Belgium**, the Act on Protection of Economic Competition controls two forms of anti-competitive behaviour: “restrictive practices” and “business concentrations”.

In respect to “restrictive practices”, the Act prohibits:

- § agreements between enterprises, decisions by associations of enterprises and concerted practices, the object or effect of which is to prevent, restrict or materially distort competition in the relevant Belgian market or a substantial part of it;
- § abuse of a dominant position in the relevant Belgian market, or a substantial part of it, by one or more enterprises.

These provisions correspond to Articles 81 EC and 82 EC. As in the European system, agreements and decisions between enterprises may be exempt from prohibition if the companies involved give notice thereof. Exemptions of this sort may be granted individually or collectively.

With regard to “business concentrations” (mergers, take-overs and creation of joint ventures), the legislation provides for presumption of control if the firms have an aggregate consolidated turnover in excess of 40 million Euros, and at least two of the firms in question each have a turnover of 15 million Euros. These two conditions are cumulative.

The concentration must be deemed permissible when the firms in question together control less than 25 per cent of the market concerned, or when the operation does not create or reinforce a dominant position that significantly impedes effective competition in the Belgian market or in a substantial part of it.

Farmers have the feeling that Belgian antitrust law functions adequately.

In contrast, farmers in **Finland** are not satisfied with the protection offered to them by their competition authority. Competition law has the effect of protecting the consumers’ interests against the farmer. Further, consumers’ interests are protected not only by the Competition Authority but also by consumer legislation and a National Consumer Authority.

Farmers in Finland feel that there should be laws to give farmers and their co-operatives better possibilities to compete with multinational giants in processing and especially in having access to the retail trade chains.

Farmers in the **USA** can take legal action under the Packers and Stockyards Act, although lawsuits are generally brought by the government. There is currently a class action suit brought by cattle producers against a large meatpacker.

Farmers consider that remedies are less than adequate under the Packers and Stockyards Act, particularly because they fail to include restitution to the harmed party.

National Farmers Union recommends the following improvements to the Packers and Stockyards Act:

1. Provision for restitution to those harmed by violations
2. Further delineation of USDA’s authority under the Packers and Stockyards Act
3. Expanding the scope of Packers and Stockyards Act with respect to poultry
4. Prohibiting packer ownership of livestock prior to slaughter

5. Requiring firm bid contracts for livestock; (i.e., prohibiting open-ended contracts)
6. Improving pricing transparency.

Farmers in the USA are barred from bringing federal lawsuits against indirect buyers and sellers that engage in harmful practices. Some states, however, allow farmers to bring legal actions against indirect buyers and sellers.

For most **developing countries**, industrial concentration in the agri-food sector is not a major concern, and hence few legal or civil remedies have been put in place. However, as the level of market liberalisation increases, farmers in developing countries are increasingly affected in their local markets by the implantation of supermarkets and their global sourcing of supplies. Farmers from the different types of farmers' organizations could come together to address such issues provided there were resources to support their mobilization and organization.

FARMER-OWNED COOPERATIVES AND ANTI-TRUST LEGISLATION

The legal position of farmer cooperatives in relation to anti-trust legislation or competition policy varies significantly throughout the world.

In **Europe**, farmer cooperatives are generally not exempt from anti-trust regulations imposed on for-profit enterprises. However, at the EU level there is a council regulation (26/62) that under certain conditions exempts agricultural co-operatives from the prohibition of cartels according to Article 81 of the Treaty of Rome. However, wide differences in the interpretation of this regulation from one member state to another create distortions of competition.

In **Uganda**, farmer-owned co-operatives are exempted from regulations imposed on for-profit enterprises.

In **Kenya**, the Co-operatives Act is under review to reflect the current state of market play. Farmers support the government strategy of encouraging formation of farmer-owned co-operatives where they do not exist and strengthening the ones that exist.

In the **USA**, the Capper-Volstead Act of 1922 gives farmers the right to form cooperatives without fear of antitrust action. As passed by Congress, the law protects cooperatives as they became organized but never gave cooperatives the right to establish monopolies with complete immunity from antitrust laws.

The advocacy for cooperatives embodied by Capper-Volstead's creation is an economic philosophy continuing today: that cooperatives offer a competitive yardstick in the business world – a measure against which to judge traditional investor-owned businesses.

INTERNATIONAL RULES ON INDUSTRIAL CONCENTRATION

Currently, there are no effective international rules governing industrial concentration in the agri-food sector.

Given the increasingly global reach of industrial concentration, farmers see a clear need for international cooperation among governments to enact and enforce worldwide competition rules. However, governments are dealing with this question as part of a broader agenda within the WTO, and most developing countries do not want to negotiate commitments in more new areas. There is also a need for a framework that promotes and defends 'ethical entrepreneurship' with respect to farmers and producers.

IFAP recognises that creating an international authority with solid responsibilities for competition policy is a very ambitious target that will be hard to obtain. However, increased collaboration among the governments in existing international institutions is essential.

Issues of anti-trust and competition laws still need further clarification to the citizens of developing countries, especially the farming community for them to be able to understand the implications of these on their activities.

OECD

The Organization for Economic Cooperation and Development (OECD) could be mandated to collect information on industrial concentration at the global level. A study could provide information on the current level of concentration, as well as on the adoption of international treaties and domestic tax laws in this area. In addition, it would be useful to have the information available on an ongoing basis, to be used in evaluating mergers of firms that do business at the international level.

An institution such as the OECD should also review the opportunity for developing standards on competition and concentration at the international level.

UNCTAD

The United Nations Conference on Trade and Development (UNCTAD) has broader representation than OECD, since it includes all the developing countries. UNCTAD's work in the area of competition law and policy to promote an understanding of the implications of any prospective multilateral competition framework should be strengthened.

RECOMMENDATIONS

Farmer-owned cooperatives

Development of farmer-owned cooperatives for marketing and processing can assist in the improvement of farmers' incomes and help to increase market share. Therefore, farmers seek a legislative framework that gives farmers and their co-operatives better

possibilities to compete with multinational giants in processing and in having access to the retail trade.

Farmer marketing boards

Producer marketing boards, established under government authority, can improve farmers' leverage in the marketplace and assist the effective marketing of farmers' product. Marketing boards can help adapt production to market requirements, help improve product quality, negotiate prices with processors and/or operate single desk marketing systems on behalf of farmers.

Control of production by non-farmer-owned corporations

IFAP opposes the production of crops and livestock by processors or marketers, whether through total ownership or financing of total operations from farm to market by vertically integrated, non-farmer-owned corporations. Farmers support legislation prohibiting such vertical integration.

Further, IFAP supports the introduction of rules which limit packer ownership of livestock. Direct or indirect ownership allows the packers to control supply in order to manipulate the market in a way that forces farmers and ranchers to receive less from the market.

It should be recognised that in developing countries most of the controls by the government went with the liberalization process that was initiated since the early 1990's. Thus a new framework for government controls in this area needs to be introduced.

Competition legislation

Effective competition provisions can enhance competition for agricultural markets and help ensure fairness, transparency, protection and bargaining rights for producers. However care must be taken to ensure that competition policy does not undermine the effective operation of producer cooperatives and marketing boards. This means that mergers of cooperatives at national level should be allowed, taking into account the small size of the internal market in many countries. Further, farmers' organisations must have the right to act collectively, in a similar way that trade unions are able to do.

At the international level, farmers seek increased cooperation among governments to develop a competition policy which controls the excesses that may arise from industrial concentration in the agri-food sector, but also respects and supports the role that cooperatives and marketing boards can play in resolving the imbalance of power between participants in the market chain.

Compulsory reporting of information on concentration

IFAP farmers urge governments to require the collection and publication of concentration information (price setting and competition, price stability, impact on agricultural structures, etc.). Firms above a certain size should be required to submit information on joint ventures and alliances between firms. In many cases, firms that are participating in joint venture arrangements behave just like firms that have merged and should be subject to the same level of antitrust scrutiny as mergers. The disclosure requirement should be

set at a threshold sufficient to include firms that account for a significant percentage of market share at a regional level.

At the international level, IFAP requests that OECD be given the responsibility to collect information, and monitor legal and institutional developments in industrial concentration in the agri-food chain, on a regular basis.

Accountability of competition authorities

Governments should require their agencies which police anti-trust issues to detail why mergers subject to antitrust review are considered acceptable, if the decision is made not to oppose the merger. This would improve accountability.

Government anti-trust agencies should require an economic impact statement whenever proposed mergers or joint ventures are reviewed which would detail the impact of such changes on farmers and ranchers prior to approval.

Level of concentration to trigger an anti-trust suit

IFAP supports establishing a level of concentration that triggers a presumption of a violation of antitrust law to make it easier for enforcement agencies to prevent high levels of concentration. This level could relate to the size of turnover of the concentrated company (“x” millions of dollars), and/or the percentage size of the share of the market concerned.

Promotional incentives

Governments should guard against the iniquitous effects of promotional incentives. As a general rule all promotional incentives, as well as short notice payments (e.g. for waste) should form part of the cost price negotiation. Where they create barriers for new firms and products to enter the market, such as ‘ slotting fees’, i.e. the large fees charged to suppliers to put their products on supermarket shelves, they should be prohibited.

Contract farming

IFAP supports family farm contract producers, and supports policies that enhance fairness and provide producers protection in their agricultural production contracts.

Specifically, IFAP supports policies which:

- Require contracts to be written in plain language and that disclose risks to producers
- Provide producers a reasonable period of time in which to review and cancel contracts
- Protect producers from contract termination out of retaliation.

§ Establishment of a ‘fast track’ commercial court, with a financial ceiling, to handle small claims from farmers related to contract disputes.

Capacity-building

IFAP urges development institutions and donor countries to give priority in their programs to building the capacity of farmers’ organisations so that they are able to meet the demands of their members, including strengthening their position in contract negotiations.