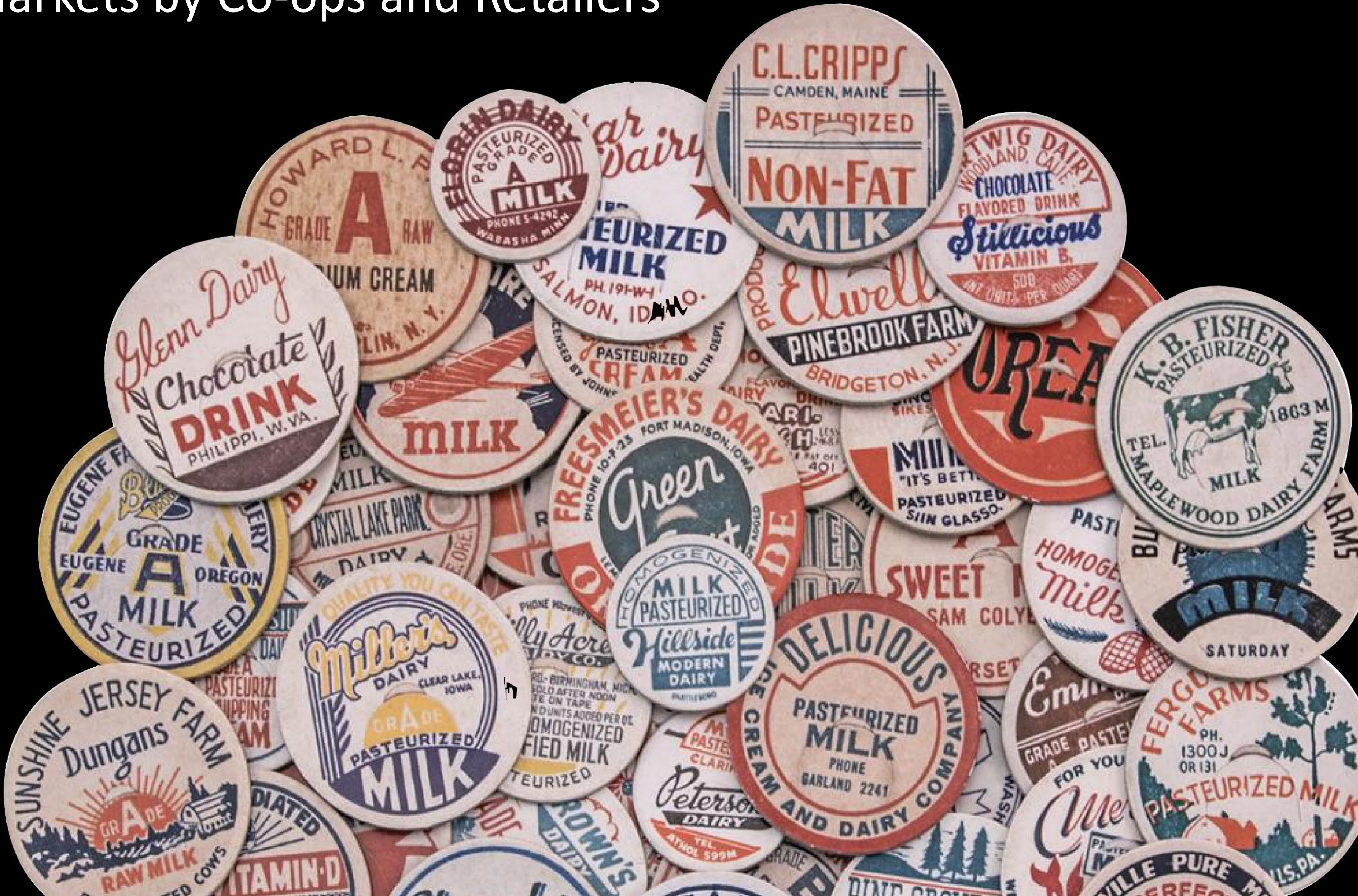
Vertical Integration and Predatory Capture of Dairy Markets by Co-ops and Retailers



Anti-Trust Laws and Old School Dairy Co-ops

Retail Imperialism

Methods of the Modern “Co-op”

Widespread Collusion

Pressure on Independent Grocery Stores

Controlling Access to Markets

Anti-Trust Laws

1890 - Sherman Antitrust Act broadly prohibits 1) anticompetitive agreements and 2) unilateral conduct that monopolizes or attempts to monopolize the relevant market. The Sherman Act triggered the largest wave of mergers in US history, as businesses realized that instead of creating a cartel they could simply fuse into a single corporation.

Note that federal laws only apply to *interstate commerce* within the United States.

Anti-Trust Laws

1914 - Clayton Act sought to capture anti-competitive practices in their incipiency by prohibiting particular types of conduct, not deemed in the best interest of a competitive market.

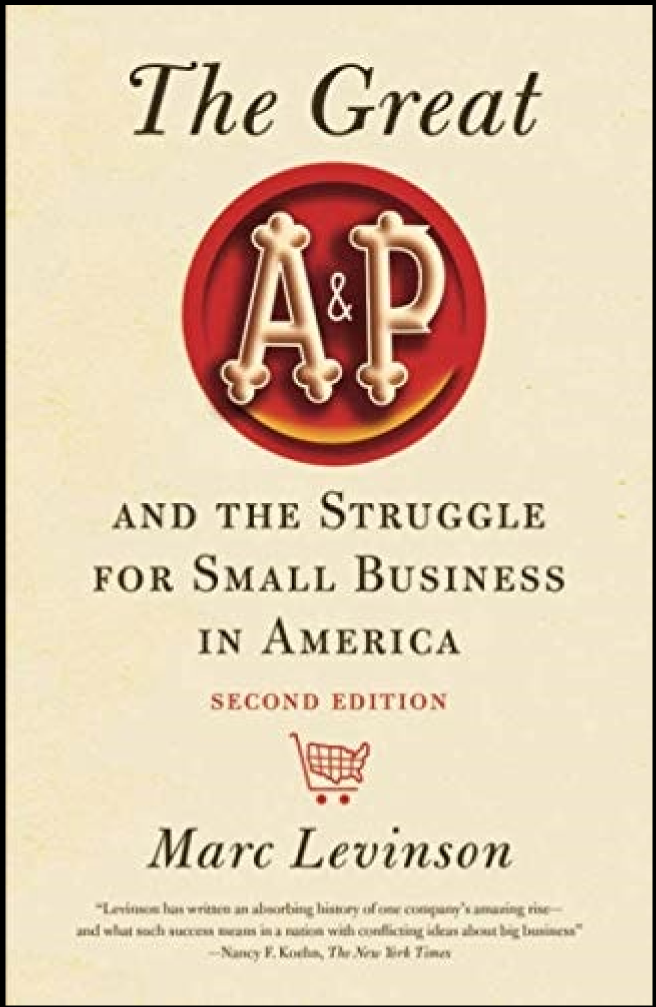
- Price discrimination to decrease competition
- Exclusive dealings and tying
- Mergers and acquisitions that *may* decrease competition
- Interlocking directorates
- Safe harbor for union activities - "labor's magna carta"

1922 - Capper–Volstead Act exempted agricultural cooperatives from anti-collusion laws to allow them to engage in a collective response to market conditions, including demand management and standard market pricing. (We'll come back to this.)

Anti-Trust Laws

1936 – Robinson-Patman Act was designed to protect small retail shops against competition from chain stores by fixing a minimum price for retail products.

Specifically, the law prevents suppliers, wholesalers, or manufacturers from supplying goods to "preferred customers" at a reduced price. It also prevents coercing suppliers into restrictions as to whom they can and can't sell goods…



…if the effect may be "substantially to lessen competition or tend to create a monopoly in any line of commerce."

Anti-Trust Laws

1950 Celler–Kefauver Act was passed to close a loophole regarding asset acquisitions and acquisitions involving firms that were not direct competitors. While the Clayton Act prohibited stock purchase mergers that resulted in reduced competition, shrewd businessmen were able to find ways around the Clayton Act simply by buying up a competitor's assets. It gave the government the ability to prevent vertical mergers and conglomerate mergers which could limit competition.

1976 - Hart–Scott–Rodino Act requires filing with the U.S. Federal Trade Commission and Department of Justice and to determine that the transaction will not adversely affect U.S. commerce under the antitrust laws.

Volstead Act and
Old School Dairy Co-ops

1922 - Capper–Volstead Act exempted agricultural cooperatives from anti-collusion laws to allow them to engage in a collective response to market conditions, including demand management and standard market pricing.

The act authorized various kinds of agricultural producers to form voluntary co-operative associations for purposes of producing, handling and marketing farm products - that is, it exempted such associations from the application of the antitrust laws – as *long as their actions benefit the members of the cooperative.*

40,000+ US dairies and processors with hundreds of dairy cooperatives

40,000+ US dairies and processors with hundreds of dairy cooperatives

Table 3—Farms and farms with milk cows, selected years[1]

Year	Total farms	Farms with milk cows[2]	Share of farms with milk cows
	Number		*Percent*
1940	6,102,417	4,663,413	76.4
1945	5,859,169	4,481,384	76.5
1950	5,388,437	3,681,627	68.3
1954	4,782,416	2,956,900	61.8
1959	3,710,503	1,836,785	49.5
1964	3,157,857	1,133,912	35.9
1969	2,730,250	568,237	20.8
1974	2,310,581	403,754	17.5
1978	2,257,775	312,095	13.8
1982	2,240,976	277,762	12.4
1987	2,087,759	202,068	9.7
1992	1,925,300	155,339	8.1
1997	1,911,859	116,874	6.1

[1]The definition of what constitutes a farm has changed through time.
[2]Farms reporting milk cow inventories at the end of the census year.

Source: *U.S. Census of Agriculture, U.S. Summary and State Data,* Volume 1, part 51, various years.

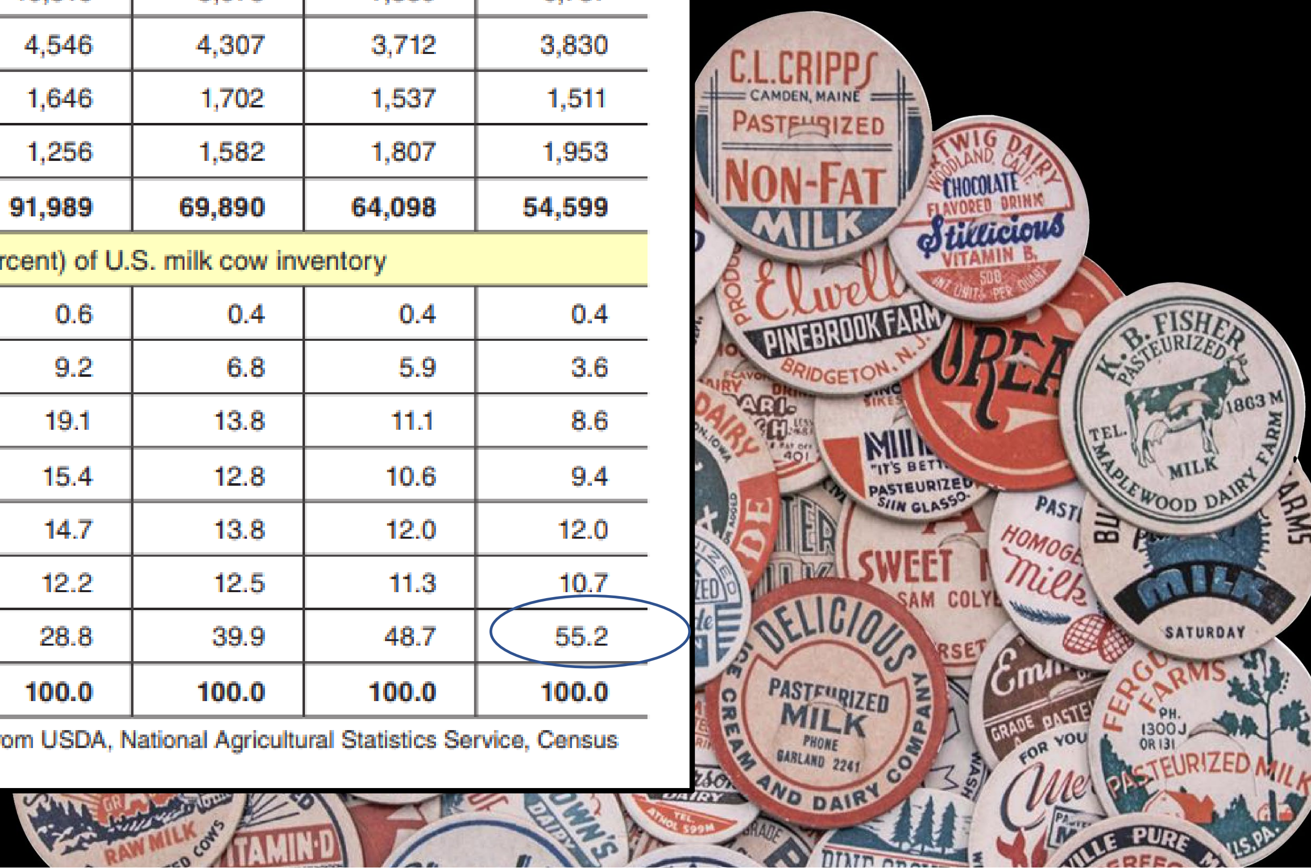
Over time, the nature of dairies and “cooperatives” changes

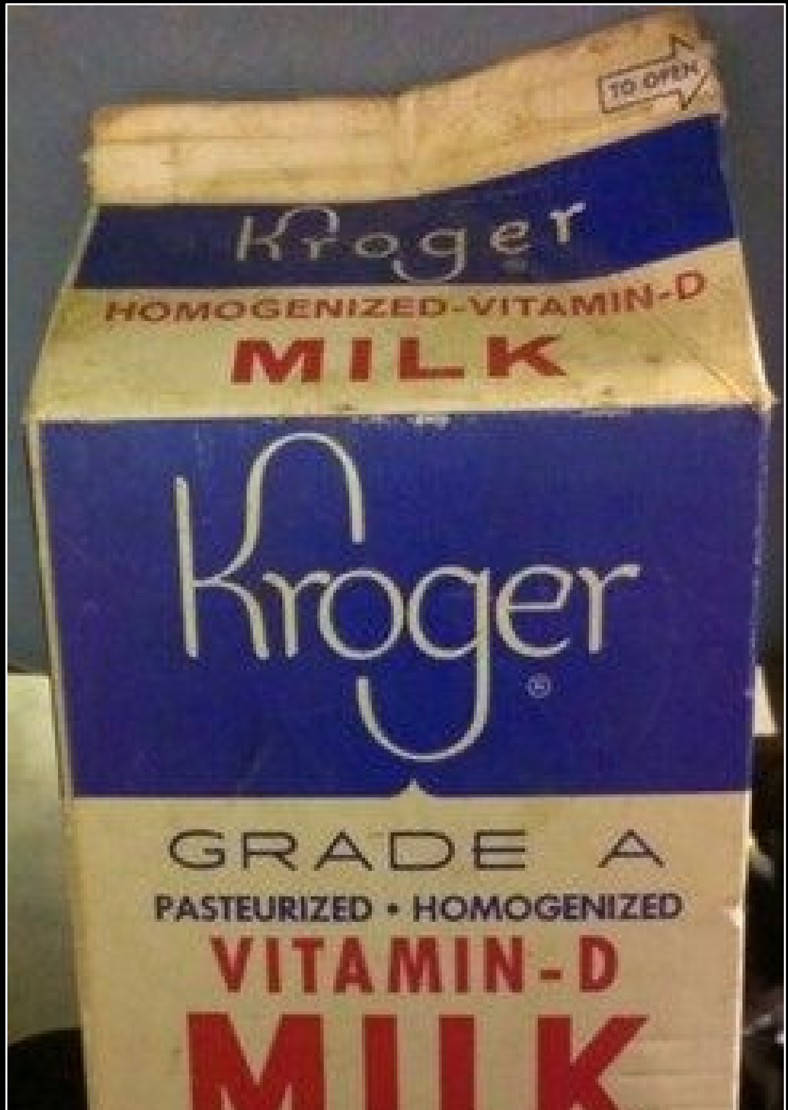
The changing size structure of U.S. dairy farms, 1992–2017

Herd size (Milk cows)	1992	1997	2002	2007	2012	2017
	Number of farms with milk cows					
1–9	32,803	22,824	21,016	14,426	16,463	16,932
10–49	60,315	40,833	27,244	19,912	17,869	11,479
50–99	41,813	33,477	25,465	18,986	15,351	12,137
100–199	14,062	12,602	10,816	8,975	7,359	6,757
200–499	4,652	4,881	4,546	4,307	3,712	3,830
500–999	1,130	1,379	1,646	1,702	1,537	1,511
>999	564	878	1,256	1,582	1,807	1,953
Total	**155,339**	**116,874**	**91,989**	**69,890**	**64,098**	**54,599**
	Share (percent) of U.S. milk cow inventory					
1–9	0.9	0.7	0.6	0.4	0.4	0.4
10–49	19.5	13.8	9.2	6.8	5.9	3.6
50–99	29.0	24.5	19.1	13.8	11.1	8.6
100–199	19.0	18.0	15.4	12.8	10.6	9.4
200–499	13.7	15.3	14.7	13.8	12.0	12.0
500–999	8.0	10.2	12.2	12.5	11.3	10.7
>999	9.9	17.5	28.8	39.9	48.7	55.2
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: USDA, Economic Research Service using data from USDA, National Agricultural Statistics Service, Census of Agriculture.

9.9% to 55% in 25 years





GROCERY DIVE

BRIEF

As large retailers process milk, dairy companies worry

Published Oct. 16, 2017

Case Study:
Kroger's Imperialism

- Stopped buying from certain dairies
- Bought competing dairies
- Produced own brand milk products
- Dictated to milker cooperatives the terms of price and delivery
- Forced small dairies to sell out or close
- Bought shuttered farms and milk plants out of bankruptcy
- Eliminated specialty products
- Began regional pooling from large milkers
  Began own regional distribution
- End of the local family dairy
- 50% rule

Case Study: Kroger's Imperialism

Hiland Dairy, Inc. v. Kroger Company August 28, 1967

The complaint alleges that Kroger has begun the construction of a dairy processing plant with sufficient capacity to supply more than 20 per cent of the total current consumer demand for dairy products in the St. Louis, Missouri, Trade Territory, "with the specific intent of supplying the full needs of all defendant's retail stores in the territory * * * [and] to sell dairy products within the relevant trade territory." Plaintiffs seek to enjoin the completion and operation of the processing plant upon the theory that if Kroger is permitted to complete and operate the plant, it will have monopoly power over dairy products in this trade territory and therefore is guilty of attempting to monopolize trade and commerce contrary to Section 2 of the Sherman Antitrust Act.

Dairy Cooperatives use their anti-trust exemption to consolidate their market control by eliminating competing cooperatives, controlling prices paid to all producers, and preventing access to markets by independent dairies.

Case Study:
Class Action Lawsuit against DFA *by its own members* for illegal practices not in the interest of all cooperative members. What was not directly specified in the complaint, but might have been exposed during discovery?

- Alleged the DFA was not acting to benefit of all coop members, so did not qualify for Volstead Act exemption
- Alleged executives of the coop maintained personal business arrangements that benefitted them exclusively
- Alleged preferential treatment of some coop members over others
- Alleged retaliation by coop execs against vocal members
- Alleged anti-competitive acts by retailers not exempted by Volstead just because they maintained membership in coop

DFA faced forced disclosure of its records and actions when it decides instead to settle for over $158 million payout to farmers.

Case Study:
Northeast Farmers vs DFA/DMS

Defendants have engaged in a multi-faceted conspiracy with processors and other cooperatives to reduce competition, acquire monopsony power, and suppress raw milk prices in the market for raw milk sales in Order 1. Defendants entered into the following explicit or inferable anticompetitive agreements: (a) agreements with other cooperatives not to compete for dairy farmers selling raw milk; (b) agreements to discourage such competition by exchanging information with other cooperatives about how much the cooperatives pay farmers for raw milk; (c) outsourcing and full supply agreements with processors to cut off raw milk outlets to independent farmers and non-conspiring cooperatives, which were coupled with most favored nations clauses to make sure that suppressed prices applied widely across processors in the market; (d) agreements to make side payments to prevent such competition for raw milk; and (e) agreements to coerce farmers who were independent or belonged to other cooperatives to join DFA in order to still have outlets for their raw milk. These agreements all anticompetitively suppressed the unregulated portion of raw milk prices paid to dairy farmers in Order 1, beginning before 2005 and continuing to the present day.

Case Study:
Northeast Farmers vs DFA/DMS

Mutual non-solicitation agreements

1. Non-Solicitation Agreements and Sharing of Farmer Pay Information.

Plaintiffs have identified disputed issues of fact as to whether DFA and other co-conspirators cooperatives entered into agreements whereby they agreed not to solicit each other's members, thereby restraining dairy farmers' ability to change cooperatives to obtain a better price for their milk. Plaintiffs have further identified disputed issues of fact as to whether DFA used its access to pay program information obtained through DMS as well as pay program information obtained from DFA's direct cooperative competitors to eliminate the likelihood a dairy farmer would achieve a better price by switching cooperative membership. Plaintiffs contend these non-solicitation agreements violated a 1977 Consent Decree and Defendants' own Antitrust Guidelines. *See* Plaintiffs' SDF ¶¶ 12-33.

Case Study:
Northeast Farmers vs DFA/DMS

Retailers and dominant cooperatives collude to prevent individual dairies from selling to other customers

2. Full Supply Agreements with Terms Exceeding One Year.

As a further overt act, Plaintiffs allege that Defendants entered into full supply agreements with processors in Order 1 which eliminated both the processor's as well as independent dairy farmers' and independent cooperative's options in the marketplace. They have proffered admissible evidence from which a rational jury could conclude that the full supply agreements in question violated a 1977 Consent Decree, Defendants' own Antitrust Policy, and in the case of Dean's Lansdale, Pennsylvania processing plants, the *Allen* settlement agreement.

Case Study:
Northeast Farmers vs DFA/DMS

Retailers and dominant cooperatives collude to offer some customers preferential pricing that does not benefit all coop members and suppressed prices overall

3. Most Favored Nation Clauses and Pricing.

In Order 1, Professor Elhauge opines that Defendants used most favored nation pricing to attract non-cooperative processors to enter into agreements at the processor level with Defendants which Defendants offset by paying dairy farmers less money for their milk. He concludes that "[t]he use of [most favored nation clauses] thus contributes to the suppression of prices across Order 1." Plaintiffs' SDF ¶ 74, Ex. Z (Elhauge Rep. at ¶ 217).

Case Study:
Northeast Farmers vs DFA/DMS

Retailers and dominant cooperatives collude to restrict access to essential dairy farm services to force dairies to comply with demands of cooperatives

4. Outsourcing Agreements.

With regard to outsourcing agreements, Plaintiffs have identified disputed issues of fact as to whether Defendants used these agreements to force independent farmers to market their milk through DFA/DMS. Because DMS provided essential milk marketing services (such as inspecting, testing, hauling, pricing, and invoicing), eliminating independent producers' and independent cooperatives' access to those services except through DFA membership allegedly left independent milk suppliers with few other options in Order 1. Although "[a] manufacturer of course generally has a right to deal, or refuse to deal, with whomever it likes, as long as it does so independently[,]" *Monsanto Co.*, 465 U.S. at 761, it cannot employ predatory means.

The result is that in most areas, dairy milkers have only one buyer for liquid milk, and that buyer favors large dairies whose business is 100% under their control.

Case Study:
DFA and the Colorado Milk Marketing Board vs Rural Retail

- DFA controls almost all hauling and purchasing of milk
- DFA can control access to veterinary, laboratory and grading services
- DFA Ft. Morgan controls all drying/evaporation/powder products
- Only 87 large dairies remain in Colorado, all near DFA in NE Colorado
- 5 main Poolers: DFA, Aurora, Safeway, Kroger, Leprino
- CMMB requires post-pasteurization price reporting – *except on DFA Ft. Morgan products and yogurt*
- $30 to access a price report using open records act request
- CMMB only allows volume discounts based on deliveries to a single site (DFA, Safeway, Kroger, Wal-Mart, Costco, and Sam's self distribute)

Rural and independent groceries therefore cannot be offered volume discounts even based on group buying programs = 20% higher prices

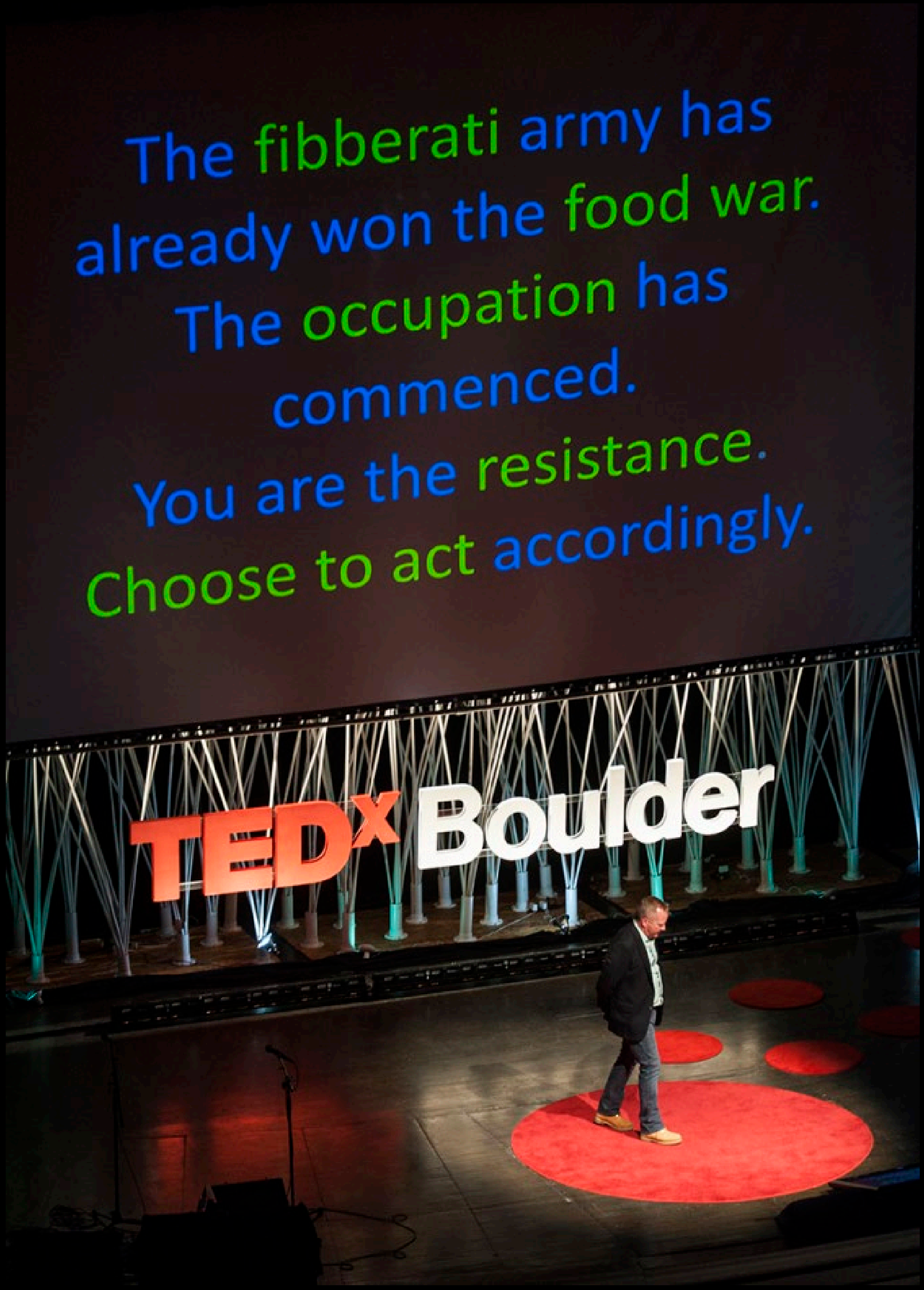
Case Study:
DFA and the Colorado Milk Marketing Board vs Rural Retail

- CMMD says “legislature gave us lawmaking and enforcement authority”
- Commissioner of Agriculture says “this is not a problem”
- State Attorney General says “appears to be legal behavior”
- Governor won’t comment, kicks it back to Dept of Agriculture
- Legislators refuse to acknowledge inquiries about CMMB
- One legislator stated, “you have no idea how powerful the DFA is, and the cost to a candidate of going up against them -- especially in an election year.”

Yet, officeholders and regulators continue to promote the promise of “rural economic vitality” as a campaign slogan.

Enforcement of the anti-monopoly laws has been primarily focused on *consumer prices* – which may in fact appear lower as the result of a large vertically integrated monopoly.

Meanwhile, collusion activity focuses on controlling producer *access to markets* – with devastating results to rural economies.



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