Executive Summary

This Captive Supply Report is in response to the mandate described in the Conference Report (House Report No. 106-948) that accompanied the 2001 Agricultural Appropriations Bill (Public Law 106-387):

> The conferees direct the Secretary of Agriculture to conduct a comprehensive study on the issue of captive supply, and deliver a report by September 30, 2001. In particular, the Secretary is instructed to examine and report on whether or not the cattle that are procured pursuant to a captive supply arrangement by a packer's non-reporting subsidiary, affiliate and owners, officers, and employees are being included in the percentages of captive supply. [1] The report shall also include the reasons why GIPSA's annual "Packers and Stockyard[s] Statistical Report" frequently reports a captive supply percentage much lower than the percentages reported by other entities.

The term "captive supply" is used throughout agriculture and other industries but has attained perhaps no greater currency than in the fed cattle industry. Simply mentioning captive supply elicits lively discussion among individuals with any vested interest in the fed cattle industry, including producers, packers, marketers, analysts, academics, regulators, and legislators. When used in the fed cattle industry, the term "captive supply" generally refers to cattle that are committed to or are owned by a packer before they are ready for slaughter. Neither practice is prohibited by the Packers and Stockyards Act of 1921, as amended (P&S Act).

Many organizations, including the United States Department of Agriculture, publish statistics commonly understood to reflect the volume of captive supply cattle procured by packers. The body of this report explains the Grain Inspection, Packers and Stockyards Administration's (GIPSA's) "captive supply" statistics as well as those by AMS and by industry organizations. The report explains GIPSA's definition of captive supply, identifies the definitions of captive supply statistics used throughout the fed cattle industry and explains why statistics collectively referred to as "captive supply" statistics do not refer to the same phenomenon. The report also sets out the results of GIPSA's verification of its 1999 captive supply statistics, including the examination of the transactional data underlying the summary information from which GIPSA's captive supply statistics were computed. Finally, the report announces actions GIPSA has taken or will take to improve the captive supply information it publishes.

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[1] Although the legislative mandate requires that Secretary to examine and report on whether or not the cattle that are procured pursuant to a captive supply arrangement *by* a packers' non-reporting subsidiaries, affiliates and owners, officers, and employees, GIPSA has interpreted the mandate to refer to cattle that are procured pursuant to a captive supply arrangement *from* a packer's non-reporting subsidiaries, affiliates and owners, officers, and employees.

Appendix A of the report provides captive supply parallels and precedents elsewhere in agriculture. It also discusses the effects that the increase in the size of packing plants and cattle feedlots has had on the marketing of cattle for slaughter. Appendix B presents the arguments supporting and opposing the use of captive supplies by both packers and producers and a summary of the economic studies that address whether the use of captive supplies affects spot market prices. Appendix C discusses captive supply and the P&S Act.

Highlights from the report are set out below.

GIPSA's Definition of Captive Supply

- GIPSA defines captive supply as livestock that is owned or fed by a packer more than 14 days prior to slaughter, livestock that is procured by a packer through a contract or marketing agreement that has been in place for more than 14 days, or livestock that is otherwise committed to a packer more than 14 days prior to slaughter.

The Definition of GIPSA's Captive Supply Statistics

- GIPSA's annual Packers and Stockyards Statistical Report provides statistics on slaughtered cattle that packers reported were packer fed or were procured through forward contracts or marketing agreements. These GIPSA statistics, and their sum as a percentage of the total cattle slaughter, have been commonly referred to and will be referred to in this report as GIPSA's captive supply statistics.

- GIPSA's captive supply statistics are based on summary data provided by packers that purchase at least $500,000 of livestock for slaughter and slaughter more than 100,000 steers and heifers a year. Packers meeting these thresholds are required to file annual reports with GIPSA with summary procurement information.

Packers' Reporting of Cattle Procured from Non-Reporting Subsidiaries, Affiliates, and Owners, Officers, and Employees

- Cattle that are procured from a packer's non-reporting subsidiary, affiliate, owner, officer, or employee are included in GIPSA's captive supply statistics if the non-reporting subsidiary, affiliate,[2] owner, officer, or employee sold the cattle through a captive supply arrangement. Purchases by a packer from its non-reporting subsidiaries, affiliates, owners, officers, or employees are not captive supply purchases simply because of the seller's status.

- GIPSA surveyed the largest 15 packers of fed cattle to determine whether they purchase cattle from non-reporting subsidiaries, affiliates, owners, officers, or

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[2] A non-reporting entity is one that does not purchase at least $500,000 of livestock for slaughter annually, and is not required to file a report.

employees. Nine of these 15 packers reported they purchase cattle from non-reporting subsidiaries, affiliates, owners, officers, or employees. Of these nine firms, six reported they purchased some of these cattle using captive supply arrangements, and all cattle purchased using these arrangements are included in the appropriate captive supply category reported to GIPSA.

- Seven of the largest 15 packers reported formal company policies prohibiting or restricting cattle feeding by owners, officers, and employees. Of the eight remaining packers, four reported a *de facto* prohibition on cattle feeding by owners, officers, and employees, seven reported making no purchases from owners or officers, and two reported purchasing a small number of cattle from employees.

GIPSA's and Other Entities' Captive Supply Statistics

- In their annual reports to GIPSA, packers are required to identify the total number of cattle they slaughtered and the number of cattle they slaughtered that they procured through methods identified in the annual report. Since 1988, GIPSA has required packers to report the number of slaughtered cattle that were 1) packer fed, or purchased through 2) fixed price or basis contracts, 3) marketing agreements, or 4) purchased more than two weeks in advance of slaughter and not reported in 1), 2), or 3).

- Based on summary procurement information filed by packers, GIPSA reports "packer fed" and "forward contract and marketing agreement" procurement information for the largest 4 and largest 15 packers that purchase steers and heifers for slaughter.

- GIPSA compared its captive supply statistics with those of USDA's Agriculture Marketing Service (AMS), Cattle-Fax, the Kansas Livestock Association, Nebraska Cattlemen, the Texas Cattle Feeders Association, and the Western Organization of Resource Councils.

- Differences between GIPSA's captive supply statistics and those reported by other organizations are attributable to differences in captive supply definitions, the data on which the statistics are based, regions, and reporting periods.

- GIPSA is the only entity that collects and reports information on *national* captive supply activity. Most significantly, GIPSA reports captive supply data defined by how packers procure cattle rather than how packers price cattle, which is how the other organizations determine captive supplies.

Verification of GIPSA's Captive Supply Statistics

- GIPSA's captive supply statistics are computed from summary information provided by packers in their annual reports. To verify the 1999 summary

information of the largest four packers, GIPSA obtained their 1999 transaction records. These transaction records are the source of the summary procurement information packers report to GIPSA.

- Based on the summary information submitted by the top four packers in their annual reports, GIPSA would have concluded that 25.2 percent of their total slaughter was procured through captive supply arrangements. Based on its review of the underlying transaction date, GIPSA has estimated that 32.3 percent of the total 1999 slaughter of the top four packers was procured through captive supply arrangements.

- Differences in reporting were caused by misunderstood or misapplied captive supply procurement category definitions and by packer tabulation errors.

GIPSA's Reporting of Captive Supply: Actions

As a consequence of this report, GIPSA has undertaken or will undertake the following actions.

- GIPSA has defined captive supply and will publish the definition in the *Federal Register*.

- GIPSA is developing a new Packer Annual Report form that will clarify reporting definitions for the various types of procurement methods by which it measures captive supply.

- GIPSA will meet with the top 15 packers to review and clarify its current reporting definitions and requirements.

- GIPSA will audit annual reports, including the information on which GIPSA computes its captive supply statistics. In conducting the audits, GIPSA will examine the data used to prepare the annual report submission, and the categorization of the data in the audited annual report.

- GIPSA will report forward contracted and marketing agreement cattle separately, consistent with applicable confidentiality restrictions.

- GIPSA will report the number of head in addition to percentages, and monthly and regional figures in addition to the annual national figures currently reported, consistent with applicable confidentiality restrictions.