(5) Requiring unreasonable additional capital investments from a poultry grower or swine production contract grower after applying the criteria in § 201.216;

(6) Failing to provide a reasonable period of time to remedy a breach of contract before termination of the contract after applying the criteria in § 201.217;

(7) Failing to provide a meaningful opportunity to participate fully in the arbitration process after applying the criteria in § 201.218;

(8) Failing to ensure accurate scales and weighing of livestock, livestock carcasses, live poultry, or feed for the purposes of purchase, sale, acquisition, payment, or settlement as required by the regulations under the Act; or

(9) Failing to ensure the accuracy of livestock, meat, and poultry electronic evaluation systems and devices for the purposes of purchase, sale, acquisition, payment, or settlement as required by the regulations under the Act.

(c) *Conduct or action that harms competition.* Absent demonstration of a legitimate business justification, any conduct or action that harms or is likely to harm competition is an ''unfair,'' ''unjustly discriminatory,'' or ''deceptive'' practice or device and a violation of section 202(a) of the Act.

■ 3. Section 201.211 is added to read as follows:

§ 201.211 Undue or unreasonable preferences or advantages.

The Secretary will consider the following criteria when determining whether a packer, swine contractor, or live poultry dealer has engaged in conduct or action that constitutes an undue or unreasonable preference or advantage and a violation of section 202(b) of the Act. These criteria include, but are not limited to:

(a) Whether a packer, swine contractor, or live poultry dealer treats one or more livestock producers, swine production contract growers, or poultry growers more favorably as compared to one or more similarly situated livestock producers, swine production contract growers, or poultry growers who have engaged in lawful communication, association, or assertion of their rights;

(b) Whether a packer, swine contractor, or live poultry dealer treats one or more livestock producers, swine production contract growers, or poultry growers more favorably as compared to one or more similarly situated livestock producers, swine production contract growers, or poultry growers who the packer, swine contractor, or live poultry dealer contends have taken an action or engaged in conduct that violates any applicable law, rule, or regulation related to the livestock or poultry operation without a reasonable basis to determine that the livestock producer, swine production contract grower, or poultry grower committed the violation;

(c) Whether a packer, swine contractor, or live poultry dealer treats one or more livestock producers, swine production contract growers, or poultry growers more favorably as compared to one or more similarly situated livestock producers, swine production contract growers, or poultry growers for an arbitrary reason unrelated to the livestock or poultry operation;

(d) Whether a packer, swine contractor, or live poultry dealer treats one or more livestock producers, swine production contract growers, or poultry growers more favorably as compared to one or more similarly situated livestock producers, swine production contract growers, or poultry growers on the basis of race, color, national origin, sex, religion, age, disability, political beliefs, sexual orientation, or marital or family status;

(e) Whether the packer, swine contractor, or live poultry dealer has demonstrated a legitimate business justification for conduct or action that may otherwise constitute an undue or unreasonable preference or advantage; and

(f) Whether the conduct or action by a packer, swine contractor, or live poultry dealer harms or is likely to harm competition.

Larry Mitchell,

Administrator, Grain Inspection, Packers and Stockyards Administration.

[FR Doc. 2016–30430 Filed 12–19–16; 8:45 am]

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DEPARTMENT OF AGRICULTURE

Grain Inspection, Packers and Stockyards Administration

9 CFR Part 201

RIN 0580–AB26

Poultry Grower Ranking Systems

AGENCY: Grain Inspection, Packers and Stockyards Administration, USDA.

ACTION: Proposed rule.

SUMMARY: The Department of Agriculture's (USDA) Grain Inspection, Packers and Stockyards Administration (GIPSA), Packers and Stockyards Program (P&SP) is proposing to amend the regulations issued under the Packers and Stockyards Act, 1921, as amended and supplemented (P&S Act). The proposed amendments will identify criteria that the Secretary may consider when determining whether a live poultry dealer's use of a poultry grower ranking system for ranking poultry growers for settlement purposes is unfair, unjustly discriminatory, or deceptive or gives an undue or unreasonable preference, advantage, prejudice, or disadvantage. The proposed amendments will also clarify that absent demonstration of a legitimate business justification, failing to use a poultry grower ranking system in a fair manner after applying the identified criteria is unfair, unjustly discriminatory, or deceptive and a violation of section 202(a) of the P&S Act regardless of whether it harms or is likely to harm competition.

DATES: We will consider comments we receive by February 21, 2017.

ADDRESSES: We invite you to submit comments on this proposed rule. You may submit comments by any of the following methods:

- *Mail:* M. Irene Omade, GIPSA, USDA, 1400 Independence Avenue SW., Room 2542A–S, Washington, DC 20250–3613.
- *Hand Delivery or Courier:* M. Irene Omade, GIPSA, USDA, 1400 Independence Avenue SW., Room 2542A–S, Washington, DC 20250–3613.
- *Internet: http://www.regulations.gov*. Follow the on-line instructions for submitting comments.

Instructions: All comments should make reference to the date and page number of this issue of the **Federal Register**. Regulatory analyses and other documents relating to this rulemaking will be available for public inspection in Room 2542A–S, 1400 Independence Avenue SW., Washington, DC 20250–3613 during regular business hours. All comments received will be included in the public docket without change, including any personal information provided. All comments will be available for public inspection in the above office during regular business hours (7 CFR 1.27(b)). Please call the Management and Budget Services staff of GIPSA at (202) 720–8479 to arrange a public inspection of comments or other documents related to this rulemaking.

FOR FURTHER INFORMATION CONTACT: S. Brett Offutt, Director, Litigation and Economic Analysis Division, P&SP, GIPSA, 1400 Independence Ave. SW., Washington, DC 20250–3601, (202) 720–7051, *s.brett.offutt@usda.gov*.

SUPPLEMENTARY INFORMATION:

Background on Prior Rulemaking

GIPSA previously published a notice of proposed rulemaking on June 22, 2010, which included requirements regarding a live poultry dealer's use of a poultry grower ranking system when determining payment for grower services. That proposed rule would have required live poultry dealers paying growers on a tournament system to pay growers raising the same type and kind of poultry the same base pay and further required that growers be settled in groups with other growers with like house types. Upon review of public comments received both in writing and through public meetings held during the comment period in 2010, we have elected not to publish this rule as a final rule, but rather have modified proposed § 201.214 and are publishing it as a proposed rule and requesting further public comment.

Background on Current Rulemaking

The P&S Act (7 U.S.C. 181 *et seq.*) sets forth broad prohibitions on the conduct of entities operating subject to its jurisdiction. For example, section 202(a) of the P&S Act prohibits packers, swine contractors, and live poultry dealers from engaging in any unfair, unjustly discriminatory, or deceptive practices. 7 U.S.C. 192(a). Section 202(b) of the P&S Act prohibits packers, swine contractors, and live poultry dealers from making or giving any undue or unreasonable preference or advantage to any particular person, or subjecting any particular person to any undue or unreasonable prejudice or disadvantage. 7 U.S.C. 192(b). These broad provisions, which have not previously been interpreted in regulations, make enforcement difficult and create uncertainty among industry participants regarding compliance.

GIPSA is proposing these regulations to clarify when certain conduct in the poultry industry related to poultry grower ranking systems violates sections 202(a) or 202(b) of the P&S Act. A poultry grower ranking system, sometimes called a ''tournament,'' is the process used by live poultry dealers to determine final payment to poultry growers upon settlement of each flock. Under a poultry grower ranking system, growers whose flocks are slaughtered during the same settlement week are paid according to a structure that compares growers' feed efficiency and live weight of the grown birds delivered to the plant. Growers with better performance according to a live poultry dealer's standards are ranked higher than growers with lower performance and, therefore, receive more compensation.

Poultry grower ranking systems are widely used by live poultry dealers operating as vertically integrated companies. The vertically integrated company is responsible for every step of the poultry production process except the raising and caring of the live birds meant for slaughter. Independent farmers, acting as contractors and referred to as ''poultry growers,'' perform this function. The vertically integrated live poultry dealer provides the chicks,[1] feed, and medication to poultry growers who house and feed the birds under a contract. The poultry grower grows the birds to market size (preferred weight for slaughter) and then, after slaughter, receives a settlement check for that flock. The payment received depends on how efficiently the poultry grower converted feed to meat as compared to the other poultry growers in the settlement group.

GIPSA has received complaints from poultry growers alleging unfair treatment in poultry grower ranking systems. Many of the underlying factors in these complaints were shared with GIPSA in the comments to the 2010 proposed rule. The 2010 proposed rule (§ 201.214) would have required live poultry dealers paying growers on a tournament system to pay growers raising the same type and kind of poultry the same base pay and further required that growers be settled in groups with other growers with like house types. Comments in favor of the proposed rule most often cited the imbalance in power and control between the poultry companies and the growers. Most common among the reasons for supporting the proposed rule was the control the poultry company has over inputs. Growers have no control over numerous inputs that ultimately determine pay. In particular, the poultry companies control the following inputs and production variables: Chick health, number of chicks placed, feed quality, medications, growout time, breed and type of bird, weighing of the birds, and weighing of the feed. Commenters complained that the poultry grower ranking system is a poor indicator of the grower's abilities and performance in growing chickens. One commenter pointed out that bird age can vary as much as 9 days in a group. Due to the relatively short growing period for poultry, there can be significant differences in bird size, and as a result, grower pay, in birds just a few days apart in age. Comments also expressed concern that company employees who are also poultry growers get preferential treatment and may get better birds or get to keep flocks longer.

Comments opposed to the proposed rule overwhelmingly cited the loss of the incentive for growers to perform. For example, commenters complained that ''there will be no incentive available for above-average growers,'' ''the pay system rewards the ones who strive to do best,'' it ''will take money from the most progressive growers,'' and ''is grossly unfair to the most productive and successful growers, only benefits the least productive and least successful.'' Those opposed to the proposed rule commented that everyone should not be paid the same, that competition is good for the industry, and that those that spend money and expend effort should be rewarded. Some commenters stated there will not be enough like houses to group together for ranking purposes.

A few commenters offered recommendations. Specifically, they suggested ''same type and kind'' of poultry should be defined as same breed, age range, sex, and target weight. Also, they suggested that the base pay rate should reflect grower's cost of production plus a reasonable rate of return. Other commenters suggested that GIPSA should clarify that incentive pay would still be allowed under the proposed rule. In GIPSA's experience reviewing live poultry dealer records, some poultry companies use the base pay as the minimum pay rate, so implementing the provision regarding base pay would not be difficult. Several comments said that ''like house type'' was poorly defined. Depending on the interpretation, there could be many different categories of like house types in which case, there could be very few growers in a given settlement group.

Commenters critical of the poultry grower ranking system focused on the live poultry dealer's control over the inputs. Inputs and other factors influencing performance and pay are not equal among growers. Commenters noted that variations in chicks, feed, and medications have a significant influence on the poultry grower's performance, but the grower has no control or influence over the quality of those inputs. As an example, one comment stated that male chickens have higher average weight gain than female chickens. Therefore, if one grower gets a higher percentage of male chickens than other growers, that grower could

[1] Poultry grower ranking systems are used extensively in broiler production. The ranking systems are also used in turkey production. References in this document to chicks, chickens, or broilers are also relevant to the use of grower ranking systems in turkey production.

have an advantage in the ranking system over growers who receive all or a higher percentage of female chickens. The breed of the poultry is also a factor. Growers who receive a breed that does not perform as well, due to the characteristics of that breed, are disadvantaged compared to growers who receive a better-performing breed. Another factor noted by commenters was the age of the breeder flock and that chicks from breeder hens that are very young or very old are known to be inferior to chicks from hens that are of prime egg-laying age. Commenters stated that poultry growers who get all or a higher percentage of chicks from very old or very young breeder hens are at a disadvantage compared to growers who receive chicks from hens in the prime weeks of laying good eggs. Citing these examples, commenters pointed out the ways live poultry dealers could give preferential treatment to some growers by delivering superior chicks to their farms.

Other comments focused on the quantity and quality of feed. One poultry grower commented about the effect on rankings when the live poultry dealer assumes that the grower receives more feed than the live poultry dealer actually delivered. The grower explained that a 200 pound under-delivery of feed in a system where production costs are averaged to ten-thousandths of a cent, would affect the rankings and cause the grower to be paid less than other growers in the settlement group. Another grower commented that he had received a delivery of bad feed that made the chickens sick. Although the live poultry dealer replaced the bad or spoiled feed, the damage had been done and the grower's flock ranked at the bottom of the poultry grower ranking for that settlement group. These commenters were expressing their frustration with the poultry grower ranking system that relied on inputs over which they had no control.

Recognizing that not all inputs are the same, in proposed new § 201.214, GIPSA is not proposing that all poultry growers receive the same quality inputs, or that growers only be ranked in settlement groups where all growers receive the same quality inputs. In each settlement group, it is very likely that the live poultry dealer will place chicks on some farms that are inferior to other chicks simply due to the variation in the birds. Likewise, feed quality or the delivery quantity may vary.

Unlike the proposed rule published in 2010 regarding poultry grower ranking systems, this proposed rule would not prohibit or prescribe certain conduct, nor would it prescribe specific payment to be made to growers. Instead, after consideration of the comments received, we are proposing a rule that encourages better sharing of information with growers and fairness in areas under a live poultry dealer's control. Proposed new § 201.214 sets forth criteria that the Secretary may consider to determine whether live poultry dealers have used the poultry grower ranking system in a manner that violates sections 202(a) or (b) of the P&S Act.

Proposed new § 201.214, ''Poultry Grower Ranking Systems'' would establish a non-exhaustive list of criteria the Secretary may consider when determining whether a live poultry dealer has violated the P&S Act with respect to the use of a poultry grower ranking system. Under proposed § 201.214(a), the Secretary may consider whether the grower is provided enough information to make informed decisions regarding the grower's poultry production operation. Such information would include the anticipated number of flocks per year and the average gross income from each flock. Because most growers borrow substantial sums of money to build and upgrade houses to meet the live poultry dealer's specifications, a grower would want a contract of sufficient length and with sufficient poultry production to repay the loan. For that reason, it is important for the poultry grower to know the anticipated average gross income from each flock in order to plan accordingly for future earnings and investments. Live poultry dealers should disclose information necessary to enable the grower to make informed decisions.

Under proposed § 201.214(b), the Secretary may consider whether a live poultry dealer supplies inputs (*e.g.,* birds, feed, and medication) of comparable quality and quantity to all poultry growers in the ranking group. When considering the inputs provided by the live poultry dealer to the poultry grower and the growout specifications established for the poultry grower, GIPSA does not require uniformity, but rather fairness among the growers in a settlement group. Growers are not paid based solely on their individual performance, but as compared to other growers in a settlement group. When a grower received inputs of either superior or inferior quality as compared to the inputs provided to other growers, that grower may be at either an advantage or disadvantage when flocks are settled depending on the quality of the inputs received. Under proposed § 201.214(b), the Secretary may also consider whether there is a pattern of supplying inferior inputs (*e.g.,* birds, feed, and medication) to one or more poultry growers in the ranking group. With regards to supplying inferior birds, as discussed above, lower quality chicks may result from very young or very old breeder hens, from a poultry breed that does not perform as well as other breeds in the growout, or for other reasons. If a poultry grower consistently receives lower quality or inferior chicks, the grower will experience higher mortality rates and lower efficiency. The grower will rank lower in the settlement group and receive less compensation as compared to the other growers in the settlement group. Similarly, if a poultry grower receives lower quality feed, or if the grower receives less feed than the quantity used to calculate payment, the grower's performance will suffer as compared to other growers in the settlement group. Also, if a grower's flock needs medication, but the live poultry dealer fails to provide the medication, or if one flock is placed on a different treatment schedule, the flock performance may suffer as compared to other flocks in the settlement group. Under proposed § 201.214(c), the Secretary may consider additional company-controlled factors that could affect a grower's performance in a settlement group.

Proposed § 201.214(d) provides that the Secretary may consider whether the live poultry dealer has demonstrated a legitimate business justification for conduct that may otherwise be unfair, unjustly discriminatory, or deceptive, or that gives an undue or unreasonable preference or advantage to any poultry grower or subjects any poultry grower to an undue or unreasonable prejudice or disadvantage. A legitimate business justification for certain conduct may be sufficient to find that the conduct does not violate the P&S Act. We request comment on the types of conduct that might be considered for a legitimate business justification, in order to give further context to this provision in the final rule.

Concurrent with the publication of this proposed rule, GIPSA is also proposing another rule in this issue of the **Federal Register** that, among other things, would clarify the conduct or action by packers, swine contractors, or live poultry dealers that GIPSA considers unfair, unjustly discriminatory, or deceptive and a violation of section 202(a) of the P&S Act. Specifically, this proposed rule includes § 201.210, ''Unfair, unjustly discriminatory, or deceptive practices or devices by packers, swine contractors, or live poultry dealers,'' which includes in paragraph (b) a non-exhaustive list of conduct or action that, absent demonstration of a legitimate business justification, GIPSA believes is unfair, unjustly discriminatory, or deceptive and a violation of section 202(a) of the P&S Act, regardless of whether the conduct harms or is likely to harm competition. Currently, proposed § 201.210(b) contains nine examples. In this rule, GIPSA is proposing to add to proposed § 201.210(b) a tenth example, § 201.210(b)(10) GIPSA also considers a live poultry dealer's failure to use a poultry grower ranking system in a fair manner after applying the criteria in § 201.214 to be an unfair, unjustly discriminatory, or deceptive practice or device and a violation of section 202(a) of the P&S Act regardless of whether it harms or is likely to harm competition.

IV. Required Impact Analyses

Executive Order 12866 and Regulatory Flexibility Act

This rulemaking has been determined to be significant for the purposes of Executive Order 12866 and, therefore, has been reviewed by the Office of Management and Budget. As a required part of the regulatory process, GIPSA prepared an economic analysis of proposed § 201.214. The first section of the analysis is an introduction and discussion of the prevalence of contracting in the poultry industry as well as a discussion of potential market failures. Next, GIPSA discusses three regulatory alternatives it considered and presents a summary cost-benefit analysis of each alternative. GIPSA then discusses the impact on small businesses.

Introduction

GIPSA issued a proposed rule on June 22, 2010, which included § 201.214. GIPSA has revised the 2010 version of § 201.214 and is now proposing a new § 201.214. The rule GIPSA proposed on June 22, 2010, included several requirements regarding live poultry dealers' use of tournament systems. That section of the proposed rule would have required live poultry dealers paying growers on a tournament system to pay growers raising the same type and kind of poultry the same base compensation and further required that growers be settled in groups with other growers with like house types. The rule also prohibited live poultry dealers from offering poultry growing arrangements containing provisions that decrease or reduce grower compensation below the base compensation amount.

Upon review of public comments received both in writing and through public meetings held during the comment period in 2010, GIPSA elected not to publish this rule as a final rule and has removed the requirements and prohibitions in the rule proposed on June 22, 2010.

GIPSA has re-written § 201.214 and is proposing this regulation to establish criteria the Secretary may consider in determining whether a live poultry dealer has used a poultry grower ranking system to compensate poultry growers in an unfair, unjustly discriminatory, or deceptive manner, or in a way that gives an undue or unreasonable preference or advantage to any poultry grower or subjects any poultry grower to an undue or unreasonable prejudice or disadvantage.[2] Coupled with § 201.3(a), which is being published as an interim final rule concurrently in this edition of the **Federal Register** and proposed § 201.210(b)(10), which is discussed below, the criteria clarify whether a live poultry dealer's use of a poultry grower ranking system violates sections 202(a) and/or 202(b) of the P&S Act.

Interim Final § 201.3(a) states that certain conduct or action can be found to violate sections 202(a) and/or 202(b) of the P&S Act without a finding of harm or likely harm to competition in all cases. Proposed § 201.210(b)(10) would add to proposed § 201.210(b), which is published as part of a separate proposed rule in this edition of the **Federal Register**, another example of conduct or action by a live poultry dealer that absent demonstration of a legitimate business justification, GIPSA considers an unfair, unjustly discriminatory, or deceptive practice or device and a violation of section 202(a) of the P&S Act regardless of whether the conduct or action harms or is likely to harm competition. Specifically, proposed § 201.210(b)(10) would clarify that absent demonstration of a legitimate business justification, GIPSA considers the failure to use a poultry grower ranking system in a fair manner after applying the criteria in proposed § 201.214 to be an unfair, unjustly discriminatory, or deceptive practice or device and a violation of section 202(a) of the P&S Act regardless of whether it harms or is likely to harm competition. Since § 201.210(b)(10) relies on the criteria in § 201.214, the estimated costs and benefits of § 201.210(b)(10) are included in the estimated costs and benefits of § 201.214.

The criteria in proposed § 201.214 would include whether a live poultry dealer has provided sufficient information to enable a poultry grower to make informed business decisions. The criteria would also address whether the inputs, including birds, feed, and medication, provided by live poultry dealers to poultry growers are of consistent quality and quantity. The criteria would recognize the non-uniformity of inputs provided by live poultry dealers to growers and discourage the live poultry dealer from consistently providing superior or inferior inputs to growers in a manner that consistently affects grower compensation. The criteria also would consider whether live poultry dealers have provided poultry growers with dissimilar production variables such as the density at which the live poultry dealer places birds, target bird sizes, and age of birds at slaughter that affects the performance and grower ranking. Finally, the criteria would consider whether a live poultry dealer has demonstrated a legitimate business justification for conduct that may otherwise be unfair, unjustly discriminatory, or deceptive or gives an undue or unreasonable preference or advantage to any poultry grower or subjects any poultry grower to an undue or unreasonable prejudice or disadvantage.

Prevalence of Poultry Contracts and Poultry Grower Ranking Systems

The production of poultry is highly vertically integrated with live poultry dealers owning or controlling most segments of the value chain. Live poultry dealers typically own the breeding stock, the hatcheries, the feedmills, the live birds, and they own and operate the slaughter operations. Live poultry dealers typically contract out the growing operations for their live birds to independent poultry growers. Live poultry dealers who own or control most segments of the value chain and contract out the growing operations of live birds are commonly referred to as integrators.[3]

Broilers are almost exclusively grown under production contracts. In 2012, 96.4% of broilers were grown under contract, while 68.5% of turkeys were grown under production contracts. Under a production contract, the live poultry dealer provides the poultry grower with many inputs including the live chicks, feed, and medications. The poultry grower in turn provides the housing, labor, water, electricity, fuel,

[2] A tournament system is a type of poultry grower ranking system.

[3] For the purposes of this Regulatory Impact Analysis, the terms live poultry dealer and integrator are used interchangeably. P&SP has jurisdiction over live poultry dealers, most of which are also integrators. The only time the Regulatory Impact Analysis will refer to integrators is when another author uses the term integrator as in Table 2.

and provides for waste removal. At the end of the grow-out period, the live poultry dealer typically picks up the birds for slaughter. The payment to the poultry grower for the growing services is often determined by a poultry grower ranking system outlined in the production contract.

Under a typical poultry grower ranking system, all growers who grew birds that were shipped to the same plant in the same week are grouped together for payment purposes. Their cost per pound of live weight is averaged using standard costs for chicks and feed. Live poultry dealers then rank the growers based on cost. Live poultry dealers typically reward growers with lower costs by providing higher compensation for their growing services. Live poultry dealers typically provide less compensation to growers with higher costs.

Contracting is an important and prevalent feature in the production of poultry. The following table shows the share of poultry, by type, produced under contract over the years that the Census of Agriculture has published data on commodities raised and delivered under production contracts.

TABLE 1—PERCENTAGE OF POULTRY RAISED AND DELIVERED UNDER PRODUCTION CONTRACTS [4]

Poultry	2002	2007	2012
Broilers (%)	98.0	96.5	96.4
Turkeys (%)	41.7	67.7	68.5

Benefits of Contracting in Agricultural Production and the Poultry Industry

Agricultural production contracts have many benefits. They help farmers and livestock producers manage price and production risks, elicit the production of products with specific quality attributes by tying prices to those attributes, and facilitate the smooth flow of commodities to processing plants encouraging more efficient use of farm and processing capacities. Agricultural production contracts can also lead to improvements in efficiency throughout the supply chain for products by providing farmers with incentives to deliver products consumers desire and produce products in ways that reduce processing costs and, ultimately, retail prices. Poultry production contracts are a specific type of agricultural production contract that are widely used due to the benefits of growing poultry under production contract arrangements.

There are benefits to both live poultry dealers and poultry growers from entering into agricultural production contracts, referred to as contract poultry growing arrangements [5] in the poultry industry. Contract poultry growing arrangements allow for a sharing of risk between the live poultry dealer and the poultry grower. Contract poultry growing arrangements have provided poultry growers with predictable income and access to financing to invest in more efficient types of houses. More efficient housing may lead to higher compensation under poultry grower ranking systems. Contract poultry growing arrangements have benefited live poultry dealers by shifting the capital expenses of growing poultry to the poultry growers.

The pervasive use of contract poultry growing arrangements has benefited the poultry industry and consumers by increasing the rate of adoption of new technology, increasing feed conversion, and increasing the ability of the industry to respond to changes in consumer demand.[6] The prevalence of contract poultry growing arrangements in the poultry industry is evidence of the benefits to growers, live poultry dealers, and consumers.

Structural Issues in the Poultry Industry

As the above discussion highlights, there are important benefits associated with the use of agriculture contracts in the poultry industry. However, if there are large disparities in the bargaining power among contracting parties resulting from size differences between contracting parties or the use of market power by one of the contracting parties, the contracts may have detrimental effects on one of the contracting parties and may result in inefficiencies in the marketplace.

For example, a contract that ties a grower to a single purchaser of a specialized commodity, even if the contract provides for fair compensation to the grower, still leaves the grower subject to default risks should the contractor fail. Another example is a contract that covers a shorter term than the life of the capital (a poultry house, for example). The grower may face the hold-up risk that the contractor (live poultry dealer) may require additional capital investments or may impose lower returns at the time of contract renewal. Hold-up risk is a potential market failure and is discussed in detail in the next section. These risks may be heightened when there are no alternative buyers for the grower to switch to, or when the capital investment is specific to the original buyer.[7] Some growers make substantial long-term capital investments as part of poultry production contracts, including land, poultry houses, and equipment. Those investments may tie the grower to a single integrator. Costs associated with default risks and hold-up risks are important to many growers in the industry. The table below shows the number of integrators that broiler growers have in their local areas by percent of total farms and by total production.

[4] Agricultural Census, 2007 and 2012. *https://www.agcensus.usda.gov/Publications/2012/Full_Report/Volume_1,_Chapter_1_US/* and *https://www.agcensus.usda.gov/Publications/2007/Full_Report/Volume_1,_Chapter_1_US/*.

[5] Under section 2(a)(9) of the P&S Act, a ''poultry growing arrangement'' is defined as ''any growout contract, marketing agreement, or other arrangement under which a poultry grower raises and cares for live poultry for delivery, in accord with another's instructions, for slaughter.''

[6] Vukina, Tomislav, ''Vertical Integration and Contracting in the U.S. Poultry Sector,'' *Journal of Food Distribution Research,* July 2001.

[7] See Vukina and Leegomonchai, *Oligopsony Power, Asset Specificity, and Hold-Up: Evidence From The Broiler Industry, American Journal of Agricultural Economics,* 88(3): 589–605 (August 2006).

TABLE 4—INTEGRATOR CHOICE FOR BROILER GROWERS [8]

Integrators in grower's area [9]	Farms	Birds	Production	Can change to another integrator
Number	Percent of total			Percent of farms
1	21.7	23.4	24.5	7
2	30.2	31.9	31.7	52
3	20.4	20.4	19.7	62
4	16.1	14.9	14.8	71
>4	7.8	6.7	6.6	77
No Response	3.8	2.7	2.7	Na

The data in the table show that 52 percent of broiler growers, accounting for 56 percent of total production, report having only one or two integrators in their local areas. This limited integrator choice may accentuate the contract risks. A 2006 survey indicated that growers facing a single integrator received 7 to 8 percent less compensation, on average, than farmers located in areas with 4 or more integrators.[10] If live poultry dealers already possess some market power to force down prices for poultry growing services, some contracts can extend that power by raising the costs of entry for new competitors, or allowing for price discrimination.[11]

Many poultry processing markets face barriers to entry, including: (1) Economies of scale; (2) high asset-specific capital costs with few alternative uses of the capital; (3) brand loyalty of consumers, customer loyalty to the incumbent processors, and high customer switching costs; and (4) governmental food safety, bio-hazard, and environmental regulations. Consistent with these barriers, there has been limited new entry.

However, an area where entry has been successful is in developing and niche markets, such as organic meat and free-range chicken. Developing and niche markets have a relatively small consumer market that is willing to pay higher prices, which supports smaller plant sizes. Niche processors are generally small, however, and do not offer opportunities to many producers or growers.

Economies of scale have resulted in large processing plants in the poultry processing industry. Barriers to entry limit the expansion of choice for poultry growers who have only one or two integrators in their local areas with no potential entrants on the horizon. The limited expansion of choice of processors by poultry growers may limit contract choices and the bargaining power of growers in negotiating contracts.

One indication of potential market power is industry concentration.[12] The following table shows the level of concentration in the poultry slaughtering industry for 2007–2015.

TABLE 5—FOUR-FIRM CONCENTRATION IN POULTRY SLAUGHTER [13]

Year	Broilers (%)	Turkeys (%)
2007	57	52
2008	57	51
2009	53	58
2010	51	56
2011	52	55
2012	51	53
2013	54	53
2014	51	58
2015	51	57

The table above shows the concentration of the four largest broiler and turkey processors has remained relatively steady at between 50 and 60 percent.

The data in Table 5 are estimates of national concentration and the size differences discussed below are also at the national level, but the economic markets for poultry may be regional or local, and concentration in regional or local areas may be higher than national measures.[14] The data presented earlier in Table 4 highlight this issue by showing the limited ability a poultry grower has to switch to a different integrator. As a result, national concentration may not demonstrate accurately the options poultry growers in a particular region actually face.

Another factor GIPSA considered in proposing § 201.214 is the contrast in size and scale between poultry growers and the live poultry dealers they supply. The disparity in size between large oligopsonistic buyers and atomistic sellers may lead to market power. The National Chicken Council states that in 2016, approximately 35 companies were involved in the business of raising, processing, and marketing chicken on a vertically integrated basis, while about 25,000 family farmers had production contracts with those companies.[15] That comes to about 714 family-growers per company. Collectively, the family-growers produced about 95 percent of the nearly 9 billion broilers produced in the United States in 2015. The other 5 percent were grown on company-owned farms. That means the average family-grower produced about 342,000 broilers. As Table 5 shows, the four largest poultry companies in the United States accounted for 51 percent of the broilers processed. That means the average volume processed by the four largest poultry companies was about 1.15 billion head, which was 3,357 times the average family grower's volume.

As the above discussion highlights, there are large size differences between poultry growers and the live poultry dealers which they supply. These size differences may contribute to unequal

[8] MacDonald, James M. Technology, Organization, and Financial Performance in U.S. Broiler Production. USDA, Economic Research Service, June 2014.

[9] Percentages were determined from the USDA Agricultural Resource Management Survey (ARMS), 2011. ''Respondents were asked the number of integrators in their area. They were also asked if they could change to another integrator if they stopped raising broilers for their current integrator.'' Ibid. p. 30.

[10] MacDonald, J. and N. Key. ''Market Power in Poultry Production Contracting? Evidence from a Farm Survey.'' *Journal of Agricultural and Applied Economics.* 44(4) (November 2012): 477–490.

[11] See, for example, Williamson, Oliver E. *Markets and Hierarchies: Analysis and Antitrust Implications,* New York: The Free Press (1975); Edlin, Aaron S. & Stefan Reichelstein (1996) ''Holdups, Standard Breach Remedies, and Optimal Investment,'' *The American Economic Review* 86(3): 478–501 (June 1996).

[12] For additional discussion see MacDonald, J.M. 2016 ''Concentration, contracting, and competition policy in U.S. agribusiness,'' *Competition Law Review,* No. 1–2016: 3–8.

[13] These data were compiled from Packers and Stockyards industry annual reports, a proprietary data source.

[14] MacDonald and Key (2012) Op. Cit. and Vukina and Leegomonchai (2006) Op. Cit.

[15] *http://www.nationalchickencouncil.org/about-the-industry/statistics/broiler-chicken-industry-key-facts/.*

bargaining power due to monopsony market power or oligopsony market power, or asymmetric information. The result is that the contracts bargained between the parties may have detrimental effects on poultry growers due to the structural issues discussed above and may result in inefficiencies in the marketplace.

Hold-Up as a Potential Market Failure

Integrators demand investment in fixed assets from the growers. One example is specific types of poultry houses and equipment the integrator may require the grower to utilize in their growing operations. These investments may improve efficiency by more than the cost of installation. Typically, the improved efficiency would accrue to both the integrator and the grower. The integrator has lower feed costs, and the grower performs better relative to other poultry growers in a settlement group. If the grower bears the entire cost of installation, then the grower should be further compensated for the feed conversion gains that accrue to the integrator. The risk is that after the assets are installed, the cost to the grower is ''sunk.'' This means that if the integrator reneges on paying compensation for the additional capital investments, and insists on maintaining the lower price, the grower will accept that lower price rather than receive nothing. This allows the integrator to get the benefit of efficiency gains, at no expense to them, with the grower bearing all of the cost. This reneging is termed ''hold-up'' in the economic literature.[16]

Hold-up can have two consequences that result in market failures. If the growers do not anticipate hold-up, then growers will spend too much on investments because the integrator who demands them is not incurring any cost. That is inefficient. If the grower does anticipate hold-up, they will act as if the integrator was going to renege even when it was not, resulting in too little investment and loss of potential efficiency gains.

Hold-up can be resolved with increased competition. If an integrator developed a reputation for reneging, and growers could go elsewhere, the initial integrator would be punished and disincentivized from reneging in the future. Unfortunately, in practice, many growers do not have the option of going elsewhere.

[16] See for example, Benjamin Klein, Robert G. Crawford, and Armen A. Alchian, ''Vertical Integration, Appropriable Rents, and the Competitive Contracting Process,'' *The Journal of Law and Economics* 21, no 2 (Oct., 1978): 297–326.

Data shown above in Table 4 indicate that there are few integrators in these markets, and that growers have limited choice. Table 5, above, indicates the level of concentration in the poultry processing industry and shows that integrators operate in concentrated markets.

This rule would allow growers to file complaints against integrators that renege, giving some of the incentive benefit of competition, without compromising the efficiency of having few large processors. In addition to addressing the potential market failure of hold-up, this rule would address inefficiencies due to incomplete and asymmetric information in poultry markets. Poultry growers who lack adequate information on the expected revenue from a growing arrangement may make inefficient investment decisions. For instance, a grower may invest too much money in building new houses or purchasing upgrades relative to what they would choose if they were fully informed about the expected return from those investments. By requiring that growers be provided sufficient information to make informed business decisions, this rule would help mitigate non-optimal investment by growers and improves social welfare.

Contracting, Industry Structure, and Market Failure: Summary of the Need for Regulation

There are benefits of contracting in the poultry industry, as well as structural issues that may result in unequal bargaining power and market failures. These structural issues and market failures would be mitigated by relieving plaintiffs from the requirement to demonstrate competitive injury. For instance, contracting parties can alleviate hold-up problems if they are able to write complete contracts, and are able to litigate to enforce the terms of those contracts when there is an attempt to engage in ex-post hold-up. Because proving competitive injury is difficult and costly, removing that burden facilitate the use of litigation by producers and growers to address violations of the Packers and Stockyards Act. If growers are able to seek legal remedies, then their contracts would be easier to enforce. This will incentivize integrators to avoid exploitation of market power and asymmetric information, as well as behaviors that result in the market failure of hold-up. The result will be improved efficiency in poultry markets. GIPSA has a clear role to ensure that market failures are mitigated so that poultry markets remain fair and competitive. Section 201.214 seeks to fulfill that role by promoting fairness and equity for poultry growers.

Cost-Benefit Analysis of the Proposed Rule

Costs of the Regulations Proposed on June 22, 2010

GIPSA issued a proposed rule on June 22, 2010, with several new regulations, many of which had the potential to impact the poultry industry. A brief summary of the regulations proposed in 2010 follows.

- Proposed § 201.3(c) stated that certain conduct may be found to violate sections 202(a) and/or 202(b) of the P&S Act without a finding of harm or likely harm to competition.
- Proposed § 201.210 would have provided specific examples of conduct that violate section 202(a) regardless of whether the conduct harms or is likely to harm competition.
- Proposed § 201.211 would have provided specific criteria the Secretary may consider when determining whether an undue or unreasonable preference or advantage or an undue or unreasonable prejudice or disadvantage has occurred in violation of section 202(b) of the P&S Act.
- Proposed § 201.213 stated that live poultry dealers obtaining poultry under a poultry growing arrangement must submit a sample copy of each unique contract or agreement to GIPSA for posting on its Web site.
- Proposed § 201.214 would have required live poultry dealers paying growers on a tournament system to pay growers raising the same type and kind of poultry the same base compensation and further required that growers be settled in groups with other growers with like house types. Proposed § 201.214 also would have prohibited live poultry dealers from offering poultry growing arrangements containing provisions that decrease or reduce grower compensation below the base compensation amount.
- Proposed § 201.215 would have provided specific criteria the Secretary may consider when determining whether a poultry grower was provided with reasonable notice prior to suspension of the delivery of birds to a poultry grower.
- Proposed § 201.216 would have set forth specific criteria the Secretary may consider when determining whether a requirement that a poultry grower make additional capital investments constitutes an unfair practice in violation of the P&S Act.
- Proposed § 201.217 would have set forth the conditions under which a poultry grower may be required to make additional capital investments.

• Proposed § 201.218 would have provided specific criteria the Secretary may consider in determining whether a live poultry dealer has provided a poultry grower a reasonable period of time to remedy a breach of contract.

• Proposed § 201.219 would have provided specific criteria the Secretary may consider when determining whether the arbitration process in a contract provides a meaningful opportunity for the poultry grower to participate fully in the arbitration process.

GIPSA considered thousands of comments before proposing the current version of § 201.214. The following provisions were in the 2010 rule, but not in the currently proposed regulation.

• Requirement that live poultry dealers paying poultry growers on a tournament system pay poultry growers raising the same type and kind of poultry the same base compensation, and that poultry growers be settled in groups with other poultry growers with like house types (§ 201.214).

• Prohibition on live poultry dealers from offering growing arrangements containing provisions that decrease or reduce poultry grower compensation below the base compensation amount (§ 201.214(a)).

• Requirement that live poultry dealers submit sample contracts to GIPSA for posting to the public (§ 201.213).

Additionally, GIPSA has adjusted the rule proposed in 2010 to give live poultry dealers more flexibility in suspending the delivery of birds and requiring capital improvements and those adjustments are reflected in current proposed §§ 201.215 and 201.216, respectively.

GIPSA is issuing § 201.3(a) as an interim final rule concurrently in this issue of the **Federal Register**. GIPSA has also revised and is currently proposing new versions of §§ 201.210 and 201.211 concurrently in a separate proposed rule in this issue of the **Federal Register**. In December 2011, GIPSA issued as a final rule §§ 201.215, 201.216, 201.217, and 201.218. Proposed § 201.217, capital investments requirements and prohibitions, was removed, and proposed §§ 201.218 and 201.219 were renumbered as §§ 201.217 and 201.218.

GIPSA has now revised § 201.214 and instead of proscribing certain conduct, new proposed § 201.214 would establish criteria the Secretary may consider in determining whether a live poultry dealer has used a poultry grower ranking system to compensate poultry growers in an unfair, unjustly discriminatory, or deceptive manner, or in a way that gives an undue or unreasonable preference or advantage to any poultry grower or subjects any poultry grower to an undue or unreasonable prejudice or disadvantage.

GIPSA received numerous comments on the proposed rule in 2010. Although many thousands of the comments submitted contained general qualitative assessments of either the costs or benefits of the proposed rule, only two comments systematically described quantitative costs across the rule's provisions.

Comments from the National Meat Association included cost estimates by Informa Economics (the Informa Study). The Informa Study estimated that the proposed rule would cost the U.S. poultry industry approximately $361.6 million.[17] The Informa Study estimated $26.0 million for the one-time direct costs of rewriting contracts, additional record keeping, etc., $33.4 million for the ongoing direct costs, and $302.2 million for cost increases due to efficiency losses.[18] However, these cost estimates assumed all of the 2010 proposed changes, many of which now do not apply.

The Informa Study recognized that the economic costs of the 2010 proposed rule would take time to materialize. The Informa Study estimated that only the direct, one-time costs would occur shortly after implementation and the more significant impacts, such as declining efficiency, would happen more slowly and would not reach the full impact until years 3 and 4 in the poultry industry after the rule become effective.[19] Thus, the $361.6 million cost estimate by the Informa Study was for when the rule reached its full impact in years 3 and 4. The Informa Study further recognized that companies would find ways to adapt to the provisions of the rule and the impact of the rule would decrease after year 4.[20]

The Informa Study posited that the several elements in the proposed rule would likely alter the integrator-grower relationship in such a way as to slow down the adoption of new technologies that increase efficiency and reduce costs.[21] The Informa Study also posited that the proposed rule would significantly increase the threat of litigation, which would reduce monetary incentives to encourage innovation and investment in new technology by growers. The resulting slowdown in investment in new and upgraded buildings would negatively impact efficiency, measured by feed conversion.

Comments from the National Chicken Council included cost estimates prepared by Dr. Thomas E. Elam, President, FarmEcon LLC (the Elam Study).[22] The Elam Study estimated that the proposed rule would cost the chicken industry $84 million in the first year increasing to $337 million in the fifth year, with a total cost of $1.03 billion over the first five years.[23] The Elam Study identified $6 million as one-time administrative costs. The study states that most of the costs would be indirect costs resulting from efficiency losses,[24] while more than half of the costs estimated would be due to a reduced rate of improvement in feed efficiency due to the proposed rule slowing the pace of innovation in the poultry industry. For litigation costs, the Elam Study concluded that the litigation costs are substantial, but unknown. Again, these cost estimates were for all of the 2010 proposed changes, many of which now do not apply.

Estimates of the costs in the Informa Study and the Elam Study were largely due to business practices that live poultry dealers were projected to alter in reaction to the proposed rule rather than changes in business practices directly imposed by the rule proposed in 2010. For example, the Elam Study expected live poultry dealers to assay (a test to determine the quality of feed) each load of feed delivered to growers to avoid litigation.[25]

GIPSA believes the cost estimates presented in the Informa Study and the Elam Study were overstated. The studies relied on interviews that queried the willingness of live poultry dealers to alter their business practices. The estimates, based on interviews, may overstate costs because the live poultry dealers would face adjustment costs from the rule proposed in 2010 and had incentives to respond that they would discontinue current practices. GIPSA also believes that certain adjustments are unlikely to occur. For example, GIPSA believes it is unlikely that live poultry dealers would take on the costly

[17] Informa Economics, Inc. ''An Estimate of the Economic Impact of GIPSA's Proposed Rules,'' prepared for the National Meat Association, 2010, Table 9, Page 53.

[18] Ibid. Page 53.

[19] Informa Economics, Inc. ''An Estimate of the Economic Impact of GIPSA's Proposed Rules,'' prepared for the National Meat Association, 2010, Page 66.

[20] Ibid, Page 67.

[21] Ibid. Page 37.

[22] See Elam, Dr. Thomas E. ''Proposed GIPSA Rules Relating to the Chicken Industry: Economic Impact.'' FarmEcon LLC, 2010.

[23] Ibid. Page 24

[24] Ibid. Page 24

[25] Elam, Page 18.

task of assaying each load of feed solely to avoid litigation.

Cost-Benefit Analysis of Proposed § 201.214

Regulatory Alternatives Considered

Executive Order 12866 requires an assessment of costs and benefits of potentially effective and reasonably feasible alternatives to the planned regulation and an explanation of why the planned regulatory action is preferable to the identified potential alternatives.[26] GIPSA considered three regulatory alternatives. The first alternative that GIPSA considered was to maintain the status quo and not propose the rule. The second alternative that GIPSA considered was revising the version of § 201.214 that GIPSA published in 2010 and proposing it as a new rule. This is GIPSA's preferred alternative as will be explained below. The third alternative that GIPSA considered was proposing a new version of § 201.214, but instituting a phased implementation of the proposed rule. Under this alternative, proposed § 201.214 would only take effect when a poultry growing contract expires, is replaced, or modified. The costs and benefits of the alternatives are discussed in order below.

Regulatory Alternative 1: Status Quo

If § 201.214 is never finalized, there are no marginal costs and marginal benefits as industry participants will not alter their conduct. From a cost standpoint, this is the least cost alternative compared to the other two alternatives. This alternative also has no marginal benefits. Since there are no changes from the status quo under this regulatory alternative, it will serve as the baseline against which to measure the other two alternatives.

Regulatory Alternative 2: The Preferred Alternative—Costs of the Proposed Rule

GIPSA expects that the direct costs of proposed § 201.214 would consist of the costs of developing a consistency management system, providing income projections to poultry growers, keeping additional records, and reviewing and re-writing poultry growing contracts to ensure that poultry grower ranking systems are not used in an unfair, unjustly discriminatory, or deceptive manner or in any way that gives an undue or unreasonable preference, advantage, prejudice, or disadvantage.

Based on its expertise regulating the poultry industry over several decades, GIPSA does not expect the proposed rule to result in a decrease in the use of poultry grower ranking systems, lower capital formation, or decreases in efficiencies in the poultry industry. The only indirect costs that GIPSA anticipates are the effects of the increase in industry costs from the direct costs on supply and demand and the resulting quantity and price impacts on the retail market for chicken and the related input market for broilers.

To estimate the costs of the proposed rule, GIPSA divided costs into two major categories, direct and indirect costs. GIPSA expects that direct costs would be comprised of administrative costs. Administrative costs include items such as the following: (1) Providing income projections to growers; (2) development of company-specific consistency management systems (CMSs) to ensure poultry grower ranking systems are not used in an unfair, unjustly discriminatory, or deceptive manner or in any way that gives an undue or unreasonable preference, advantage, prejudice, or disadvantage; (3) additional record keeping; (4) review of written contracts by attorneys and the employees of regulated companies; and (5) all other administrative office work associated with review of contracts.

Indirect costs include costs caused by changes in supply and/or demand resulting from the proposed rule. Indirect costs also include potential efficiency losses due to potential changes in poultry grower ranking systems.

Regulatory Alternative 2: Direct Costs—Administrative Costs

To estimate administrative costs of the proposed rule, GIPSA relied on its experience reviewing the operations and business records of live poultry dealers, poultry growing contracts, and other business records for compliance with the P&S Act and regulations. GIPSA also considered the impact of each criterion contained in § 201.214 on administrative costs.

Under § 201.214(a), the Secretary may consider whether a live poultry dealer has provided sufficient information to a poultry grower to enable the poultry grower to make informed business decisions. Such information should include information necessary to calculate the expected income from the poultry growing arrangement. Current poultry growers who have been compensated for multiple flocks under a poultry grower ranking system may already have sufficient information because they have already established income patterns by participating in the poultry grower ranking system. The criterion in proposed § 201.214(a) would mainly apply to new growers, those growers switching to different live poultry dealers, or to growers considering housing upgrades where this information is not already available to the poultry grower.

In the past, live poultry dealers commonly provided prospective growers with projection sheets that would provide a grower with estimates of the minimum and maximum compensation they could expect under a contract. GIPSA's experience conducting investigations and compliance reviews in the poultry industry has indicated that not all live poultry dealers currently provide projection sheets to poultry growers.

GIPSA expects that it would not be difficult for live poultry dealers to develop and provide projection sheets for each contract type to all current and prospective growers. GIPSA believes that providing projection sheets to growers that contained the minimum, average, and maximum compensation they can expect for the contract type they are considering or under which they are currently growing would be sufficient information to enable the poultry growers to make informed business decisions about their future compensation and whether the compensation is sufficient to warrant increasing capital investments, for example.

Based on GIPSA's experience regulating live poultry dealers and reviewing their records, it developed time estimates for the number of hours for company managers and information technology (IT) staff to develop new projection sheets or review and revise existing sheets for each type of poultry growing contract that contains a poultry grower ranking system on which to base grower compensation. GIPSA estimates that there are 10 individual contract types for each of the 133 live poultry dealers who report to GIPSA. GIPSA also developed time estimates for legal staff to review the projection sheets and for the company to deliver the projection sheets to all current and prospective growers. GIPSA estimates that each projection sheet for each of the 1,330 unique contract types would take eight hours of management and IT time to prepare, and two hours of attorney time to review and rewrite the contract. In addition, it will take 0.2 hours of administrative time to print, and mail the projection sheets and revised contracts for each of the 21,925 individual poultry production contracts of which GIPSA is aware. GIPSA multiplied the estimated hours to conduct these tasks by the average

[26] See Section 6(a)(3)(C) of Executive Order 12866.

hourly wages for managers and IT staff at $58/hour, attorneys at $83/hour, and administrative assistants at $34/hour as reported by the U.S. Bureau of Labor Statistics in its Occupational Employment Statistics.[27] GIPSA estimates the development and delivery of projection sheets to cost the poultry industry $0.99 million.

The criterion in § 201.214(b) permits the Secretary to consider whether a live poultry dealer supplies inputs of comparable quality and quantity to all poultry growers in the ranking group and whether there is a pattern or practice of supplying inferior inputs to one or more poultry growers in the ranking group. Inputs include birds, feed, medication, and any other input supplied by the live poultry dealer.

The U.S. Food and Drug Administration (FDA) approves all medication that can be administered to broilers that are grown for human consumption.[28] GIPSA believes that live poultry dealers would not alter medication to such an extent that inferior medicine is consistently supplied to a grower and that this criterion would not be costly to the industry.

GIPSA also believes that feed provided by live poultry dealers would be consistent across a group of growers and that this criterion would not be costly to the industry. Feed is produced by live poultry dealers at a feedmill and the same batch of feed is distributed to growers until more feed is produced and then that feed is distributed. The process of the production and distribution of feed ensures consistency across the group of growers that receive the same batch of feed. Once a batch of feed is produced, live poultry dealers truck it to growers according to established routes and schedules. All growers on the same route should receive feed of similar quality.

The chicks supplied by a live poultry dealer to a poultry grower have the potential to be inconsistent and GIPSA believes that live poultry dealers would have to take action to ensure a poultry grower is not consistently supplied with inferior chicks. The factors that affect chick quality include the age and breed of the breeder stock and the conditions at the hatchery. Hatchery conditions affecting chick quality include, hatching egg quality, time of collection, egg storage temperature and humidity, incubation temperature, incubator carbon dioxide concentration, and chick hatching time in relation to being removed from the incubator.[29]

It is possible that the rotation of chicks being hatched and delivered could result in the same grower(s) receiving inferior chicks on a consistent basis. In order to avoid the possibility of consistent placement of inferior chicks with the same grower, even if unintentional, live poultry dealers would likely respond by designing and implementing a CMS to identify and evenly distribute inferior chicks.

GIPSA expects the same CMS to be used to demonstrate that a poultry grower ranking system is not used in an unfair, unjustly discriminatory, or deceptive manner, or in a way that gives an undue or unreasonable preference or advantage to any poultry grower or subjects any poultry grower to an undue or unreasonable prejudice or disadvantage. Proposed § 201.214(c) would allow the Secretary to consider whether a live poultry dealer provides poultry growers with dissimilar production variables in the ranking group in a manner that affects a poultry grower's compensation. Production variables include, but are not limited to, the density at which the live poultry dealer places birds, the target slaughter weights of the birds, and bird ages that vary by more than seven days. The live production and broiler management teams must work together to ensure that medication, bird densities, target bird sizes, and the timing of the harvesting of flocks does not consistently affect grower rankings. Each live poultry dealer, whether large or small, would need to design and implement one CMS to cover all of its breeding, hatching, feedmill, and broiler operations. This CMS would ensure that growers are not treated inconsistently and that there is not a pattern or practice of unfair, unjustly discriminatory, or deceptive treatment or undue or unreasonable preference, advantage, prejudice, or disadvantage.

GIPSA relied on its knowledge of the poultry industry to estimate the cost of designing and implementing a CMS that could be used by both large and small live poultry dealers. GIPSA estimates that it would take 640 hours of management and IT staff time to develop a CMS. GIPSA estimates it would take 8 hours per live poultry dealer for its legal team to review the CMS and 96 hours to train the breeding, hatching, and broiler staff how to use the CMS to ensure the uniform distribution of inferior chicks. GIPSA multiplied the estimated hours to conduct these tasks by the average hourly wages for managers and IT staff at $58/hour, attorneys at $83/hour, and administrative assistants at $34/hour as reported by the U.S. Bureau of Labor Statistics in its Occupational Employment Statistics.[30] GIPSA estimates that if all 133 live poultry dealers who report operations to GIPSA develop and implement a CMS, the cost would total $5.46 million. This estimate overstates the cost because some of the 133 live poultry dealers do not use a poultry grower ranking system. Rather than risk underestimating the potential cost, GIPSA chose to include all 133 live poultry dealers in the calculations. We have not estimated any capital costs associated with the creation and implementation of a CMS, as we believe that there are none or existing equipment would be used; however, we seek comment on the validity of this assumption and if commenters disagree with it, to provide estimates of the capital costs.

Each live poultry dealer that uses a poultry grower ranking system to calculate grower compensation would need to keep additional records to demonstrate that poultry grower ranking systems are used in a fair manner after applying the criteria in proposed § 201.214. Proposed § 201.214(d) allows the Secretary to consider whether a live poultry dealer has demonstrated a legitimate business justification for use of a poultry grower ranking system in a manner that may otherwise be unfair, unjustly discriminatory, or deceptive or gives an undue or unreasonable preference or advantage to any poultry grower or subjects any poultry grower to an undue or unreasonable prejudice or disadvantage.

Based on GIPSA's knowledge and review of records kept by live poultry dealers, GIPSA believes that the live poultry dealers already keep very detailed records regarding the performance of each grower. The records include all information needed to calculate feed conversion such as weights and quantities of inputs provided, and all other data used to determine grower performance and compensation. Based on GIPSA's experience reviewing these records and the business operations of live poultry dealers, GIPSA estimates that live poultry dealers will spend an additional 8 hours of time preparing records for

[27] All salary costs are based on mean annual 2015 salary adjusted for benefit costs, set to an hourly basis. *http://www.bls.gov/oes/*. Accessed on August 26, 2016.

[28] *http://www.accessdata.fda.gov/scripts/animaldrugsatfda/*. Accessed on August 26, 2016.

[29] The University of Georgia Cooperative Extension Service, ''Hatchery Breeder Tip . . . Chick Quality: An Update,'' May 2005.

[30] All salary costs are based on mean annual 2015 salary adjusted for benefit costs, set to an hourly basis. *http://www.bls.gov/oes/*. Accessed on August 26, 2016.

each poultry contract in order to be able demonstrate that the poultry grower ranking system is used in a fair manner after applying the criteria in proposed § 201.214. GIPSA has data on the number of production contracts between poultry growers and live poultry dealers. GIPSA multiplied 8 hours of time by the average hourly wages of $34/hour as reported by the U.S. Bureau of Labor Statistics in its Occupational Employment Statistics [31] and then multiplied this total by the 21,925 individual poultry growing contracts reported to GIPSA by live poultry dealers to arrive at $5.96 million for additional record keeping costs for live poultry dealers. This record keeping estimate includes keeping records to demonstrate legitimate business justifications for proposed § 201.214(d).

Given that proposed § 201.214 is a new regulation, live poultry dealers would need to review the contractual language in their existing contracts with respect to poultry grower ranking systems to ensure that they are used in a fair and non-preferential manner after applying the criteria in proposed § 201.214. GIPSA again relied on its experience and developed time estimates for the number of hours for attorneys and company managers to review and revise verbal and written production contracts and for staff to make changes, copy, and obtain signed copies of the contracts. For poultry growing contracts, GIPSA estimates that each of the 1,330 unique contract types would take 2 hours of attorney time and 2 hours of company management time to review and rewrite, and it would take 2 hours of administrative time to review each of the 21,925 individual poultry production contracts. GIPSA multiplied the estimated hours to conduct these administrative tasks by the average hourly wages for attorneys at $83/hour, managers at $58/hour, and administrative assistants at $34/hour as reported by the U.S. Bureau of Labor Statistics in its Occupational Employment Statistics.[32]

GIPSA recognizes that contract review costs would also be borne by poultry growers. GIPSA estimates the each grower would spend 1 hour of time reviewing a contract and would spend 1 hour of their attorney's time to review the contract. GIPSA multiplied 1 hour of grower time and 1 hour of attorney time to conduct the production contract review by the average hourly wages for attorneys at $83/hour and managers at $58/hour. GIPSA then applied this cost to the 21,925 poultry growing contracts that have been reported to GIPSA to arrive at the total contract review costs that would be incurred by poultry growers. GIPSA then added together the contract review costs by live poultry dealers and by poultry growers to arrive at estimated contract review costs of $4.96 million for the poultry industry.

GIPSA then added together all of the estimated types of administrative costs and the estimated first-year total administrative costs appear in the following table:

TABLE 4—FIRST-YEAR ADMINISTRATIVE COSTS OF PROPOSED § 201.214

Administrative cost type	$ millions
Projection Sheet Costs	0.99
Develop Consistency Management System	5.46
Industry Record Keeping	5.96
Contract Review Costs	4.96
Total Industry Administrative Cost	17.37

The first-year total administrative costs would be $17.37 million for the poultry industry. The two largest costs would be industry record keeping and the development of CMSs, followed by record keeping and the costs of developing projection sheets.

A. Regulatory Alternative 2: Direct Costs—Litigation Costs of the Preferred Alternative

Interim final regulation 201.3(a) will already be in effect if and when § 201.214 becomes effective. GIPSA expects that § 201.3(a) will result in additional litigation as this rule states that certain conduct or action can violate sections 202(a) and/or 202(b) of the P&S Act without a harm or likely harm to competition in all cases. Section 201.3(a) formalizes GIPSA's longstanding position that, in some cases, violations of sections 202(a) and 202(b) can be proven without demonstrating harm or likely harm to competition. Section 201.214 provides clarity to the industry by establishing criteria the Secretary may consider in determining whether a live poultry dealer has used a poultry grower ranking system to compensate poultry growers in an unfair, unjustly discriminatory, or deceptive manner, or in a way that gives an undue or unreasonable preference or advantage to any poultry grower or subjects any poultry grower to an undue or unreasonable prejudice or disadvantage.

Regulation 201.3(a) is broad in nature. Section 201.214 simply provides clarity and GIPSA believes that § 201.214 will not lead to litigation above that already expected as a result of § 201.3(a). Thus, GIPSA considers the additional litigation under § 201.3(a) to be the baseline litigation costs for § 201.214 and that the litigation costs for § 201.3(a) already include the litigation costs of § 201.214. Since those litigation costs have already been counted under § 201.3(a), GIPSA does not allocate any additional litigation costs to § 201.214 and for the purposes of this RIA, the marginal litigation costs are zero.

Regulatory Alternative 2: Total Direct Costs of the Preferred Alternative

The total first-year direct costs of proposed § 201.214 would consist of administrative and litigation costs (which are equal to zero) from above and they are summarized in the following table.

TABLE 5—DIRECT COSTS OF PROPOSED § 201.214

Cost type	($ millions)
Admin Costs	17.37
Litigation Costs	0.00
Total Direct Costs	17.37

GIPSA estimates that the direct costs of proposed § 201.214 would be $17.37 million.

Regulatory Alternative 2: Indirect Costs of the Preferred Alternative

As discussed previously, GIPSA does not expect proposed § 201.214 to result in a decrease in the use of poultry grower ranking systems, lower capital formation, or decreases in efficiencies in the poultry industry. The regulation simply establishes the criteria under which the Secretary may determine whether live poultry dealers are using poultry grower ranking systems in an unfair, unjustly discriminatory, or deceptive manner, or in a way that gives an undue or unreasonable preference or advantage to any poultry grower or subjects any grower to an undue or unreasonable prejudice or disadvantage.

The only indirect costs that GIPSA anticipates are the effects of the increase in industry costs from the direct administrative costs on supply and demand, and the resulting quantity and price impacts on the retail market for chicken and the related input market for broilers.

GIPSA modeled the impact of the increase in total industry costs resulting from the direct costs of proposed § 201.214 in a Marketing Margins Model

[31] Ibid.

[32] All salary costs are based on mean annual 2015 salary adjusted for benefit costs, set to an hourly basis. *http://www.bls.gov/oes/*. Accessed on August 26, 2016.

(MMM) framework.[33] The MMM allows for the estimation of changes in consumer and producer surplus and the quantification of deadweight loss or gain caused by changes in supply and demand conditions in the retail market for chicken as well as the input market for poultry growing services.

GIPSA modeled the increases in industry costs resulting from higher direct costs as an inward (or upward) shift in the supply curve for chicken. This has the effect of increasing the equilibrium prices and reducing the equilibrium quantity traded. This also has the effect of reducing the derived demand for poultry growing services, which causes a reduction in the equilibrium prices and quantity traded. Established economic theory suggests that these shifts in the supply curve and derived demand curve and the resulting price and quantity impacts will result in a reduction in social welfare through a deadweight loss.

To estimate the output and input supply and demand curves for the MMM, GIPSA constructed linear supply and demand curves around equilibrium price and quantity points using price elasticities of supply and demand from the USDA's Economic Research Service.[34]

GIPSA then shifted the supply curve for chicken up by the amount of the increase in total costs for the poultry industry from Table 5 above. GIPSA calculated the new equilibrium price and quantity traded of chicken. GIPSA also calculated the new equilibrium price and quantity in the poultry growing services market resulting from the decreases in derived demand for growing services. GIPSA calculated the resulting social welfare changes in the input and output markets.

The calculation of the price impact from the increase in poultry industry costs from proposed § 201.214 would have in a price increase of approximately two-hundredths of a cent in the retail price of chicken.[35] This is because the increase in total industry costs is very small in relation to overall industry costs. The result is that the resulting deadweight losses from the increases in total industry costs is indistinguishable from zero and therefore, GIPSA concludes that the indirect costs of proposed § 201.214 are zero.

Regulatory Alternative 2: Total Costs of the Preferred Alternative

GIPSA added all direct costs to the indirect costs, which are equal to zero, to arrive at the estimated total first-year costs of proposed § 201.214. The total costs are summarized in the following table.

TABLE 6—TOTAL COSTS OF PROPOSED § 201.214

Cost type	($ millions)
Admin Costs	17.37
Litigation Costs	0.00
Total Direct Costs	17.37
Total Indirect Costs	0.00
Total Costs	17.37

GIPSA estimates that the total costs of proposed § 201.214 to be $17.37 million for the poultry industry in the first full year of implementation

Regulatory Alternative 2: 10-Year Total Costs of the Preferred Alternative

To arrive at the estimated 10-year costs of proposed § 201.214, GIPSA expects the costs to be constant for the first 5 years while courts are setting precedents for the interpretation of proposed § 201.214 if indeed it is finalized. GIPSA expects that case law with respect to proposed § 201.214 would be settled after 5 years, and by then, industry participants would likely know how GIPSA would enforce the proposed regulation and how courts would interpret the proposed regulation if finalized. The effect of courts establishing precedents is that administrative costs would likely decline after 5 years.

Once courts establish precedents in case law, GIPSA expects the direct administrative costs of reviewing and revising contracts and developing projection sheets would decrease rapidly as contracts would already contain any language modifications necessitated by implementation of the proposed rule, and projection sheets would already have been developed for most contracts. GIPSA also expects that the direct costs of record keeping and operating CMSs would decrease rapidly as courts set precedents on which records would be required and how detailed a CMS must be, and as companies become more efficient in ensuring that poultry grower ranking systems are used in a fair manner after applying the criteria in proposed § 201.214.

To arrive at the estimated 10-year costs of proposed § 201.214, GIPSA estimates that contracts would expire at a steady rate. Based on its expertise, GIPSA believes that 20 percent of contracts would expire on a yearly basis and thus, in the first five years, 20 percent of all contracts would expire and need to be renewed each year or new production contracts would be put in place. Thus in years 2 through year 5, contract review costs would be 20 percent of the costs of review in the first year because the costs of reviewing and revising contracts would only apply to the 20 percent of contracts that are expiring or are new contracts each year. Based on GIPSA's expertise, GIPSA also estimates that in years 2 through year 5, 20 percent of all projection sheets would require updating each year, the cost of operating and updating CMSs would be 20 percent of first-year development costs, and that record keeping costs would be 20 percent of the first-year cost as companies become more efficient in record keeping and learn which records are required. Based on its expertise, GIPSA estimates that in the second 5 years, the direct administrative costs of revising contracts, projection sheets, CMS operation, and record keeping would decrease by 50 percent per year as the courts establish precedents, contracts would contain standard language, and companies would become more efficient at ensuring poultry grower ranking systems are used in a fair manner after applying the criteria in proposed § 201.214. The total 10-year costs of proposed § 201.214 appear in the table below.

TABLE 7—TEN-YEAR TOTAL COSTS OF PROPOSED § 202.214

Year	Total direct ($ millions)
2018[36]	17.37
2019	3.47
2020	3.47
2021	3.47
2022	3.47
2023	1.74
2024	0.87
2025	0.43
2026	0.22
2027	0.11
Totals	34.64

Based on the analysis, GIPSA expects the 10-year total costs of proposed § 201.214 would be $34.64 million.

[33] The framework is explained in detail in Tomek, W.G. and K.L. Robinson "*Agricultural Product Prices,*" third edition, 1990, Cornell University Press.

[34] ERS Price Elasticities: *http://www.ers.usda.gov/data-products/commodity-and-food-elasticities/demand-elasticities-from-literature.aspx.* Accessed on August 26, 2016.

[35] The $17.37 million increase in total industry costs from proposed § 201.214 is only 0.04 percent of total poultry industry costs of approximately $40 billion.

[36] GIPSA uses 2018 as the date for the proposed rule to be in effect for analytical purposes only. The date the proposed rule becomes final is not known.

Regulatory Alternative 2: Net Present Value of Ten-Year Total Costs of the Preferred Alternative

The total costs of proposed § 201.214 in the table above show that the costs are highest in the first year, decline to a constant lower level over the next 4 years, and then gradually decrease again over the subsequent 5 years. Costs to be incurred in the future are less expensive than the same costs to be incurred today. This is because the money that is used to pay the costs in the future can be invested today and earn interest until the time period in which the cost is incurred. After the cost has been incurred, the interest earned would still be available.

To account for the time value of money, the costs of the regulations to be incurred in the future are discounted back to today's dollars using a discount rate. The sum of all costs discounted back to the present is called the net present value (NPV) of total costs. GIPSA relied on both a three percent and seven percent discount rate as discussed in Circular A–4.[37] GIPSA measured all costs using constant dollars.

GIPSA calculated the NPV of the ten-year total costs of the proposed regulation using both a three percent and seven percent discount rate and the NPVs appear in the following table.

TABLE 8—NPV OF TEN-YEAR TOTAL COSTS OF PROPOSED § 201.214

Discount rate	($ millions)
3 Percent	32.16
7 Percent	29.36

GIPSA expects the NPV of the 10-year total costs of § 201.214 will be $32.16 million at a three percent discount rate and $29.36 million at a seven percent discount rate.

Regulatory Alternative 2: Annualized Costs of the Preferred Alternative

GIPSA then annualized the NPV of the 10-year total costs (referred to as annualized costs) of proposed § 201.214 using both a three percent and seven percent discount rate as required by Circular A–4 and the results appear in the following table.[38]

[37] *https://www.whitehouse.gov/sites/default/files/omb/assets/regulatory_matters_pdf/a-4.pdf.* Accessed on August 26, 2016.

[38] Ibid.

TABLE 9—ANNUALIZED COSTS OF PROPOSED § 201.214

Discount rate	($ millions)
3 Percent	3.77
7 Percent	4.18

GIPSA expects that the annualized costs of § 201.214 would be $3.77 million at a three percent discount rate and $4.18 million at a seven percent discount rate.

Impacts on Costs of Interim Final § 201.3(a)

Concurrent with proposing § 201.214, GIPSA is issuing an interim final version of § 201.3(a). Section 201.3(a) states that conduct or action can be found to violate sections 202(a) and/or 202(b) of the P&S Act without a finding of harm or likely harm to competition in all cases. As a stand-alone regulation, § 201.3(a) formalizes GIPSA's longstanding position that, in some cases, violations of sections 202(a) and 202(b) can be proven without demonstrating harm or likely harm to competition.

In its Regulatory Impact Analysis, GIPSA estimated the annualized costs of § 201.3(a) would range from $6.87 million to $96.01 million at a three percent discount rate and from $7.12 million to $98.60 million at a seven percent discount rate. The range of potential costs is broad and GIPSA relied on its expertise to arrive at a point estimate of expected annualized costs. GIPSA expects the cattle, hog, and poultry industries to primarily take a ''wait and see'' approach to how courts will interpret § 201.3(a) and only slightly adjust its use of AMAs, and incentive or performance-based payment systems. GIPSA estimates that the annualized costs of § 201.3(a) at the point estimate will be $51.44 million at a three percent discount rate and $52.86 million at a seven percent discount rate based on an anticipated ''wait and see'' approach by the cattle, hog, and poultry industries.

GIPSA recognizes that courts, after the implementation of a finalized § 201.3(a), may opt to continue to apply earlier precedents of requiring the showing of harm or potential harm to competition in section 202(a) and 202(b) cases. This has the potential to affect the costs of § 201.214 and 201.211 should they become finalized. GIPSA expects that even if courts continue to require showing of harm or potential harm to competition in section 202(a) and 202(b) cases, that firms would likely still incur costs of complying with § 201.214. Even if regulated entities expect that courts would require showing of a harm to competition for § 201.214 violations, the regulated entities may still expect litigation as private parties test the courts application of § 201.3 as it relates to § 201.214 violations. To reduce this threat of litigation, regulated entities may still incur the administrative costs detailed above. Should § 201.214 become finalized and courts still require a showing of harm or potential harm to competition, regulated entities may still voluntarily undertake the adjustment costs detailed above.

GIPSA expects proposed § 201.214 to reduce the costs of implementing § 201.3 by providing more clarity in the appropriate application of sections 202(a) and (b) of the P&S Act as they apply to poultry grower ranking systems. Section 201.214 provides clarity to the industry by establishing criteria the Secretary may consider in determining whether a live poultry dealer has used a poultry grower ranking system to compensate poultry growers in an unfair, unjustly discriminatory, or deceptive manner, or in a way that gives an undue or unreasonable preference or advantage to any poultry grower or subjects any poultry grower to an undue or unreasonable prejudice or disadvantage.

Regulatory Alternative 2: Benefits of the Preferred Alternative

GIPSA was unable to quantify all the benefits of proposed § 201.214. However, there are a number of important qualitative benefits of proposed § 201.214 that merit discussion. Proposed § 201.214 contains several provisions that GIPSA expects would improve efficiencies and reduce market failures. For regulations to improve efficiencies for market participants and generate benefits for consumers and producers, they must increase the amount of relevant information to market participants, reduce information asymmetries, protect private property rights, or foster competition.

Proposed § 201.214(a) would reduce information asymmetries and result in poultry growers making informed business decisions such as whether to enter the industry and in which capital improvements to invest. Growers having more complete information would result in more efficient levels of capital in the growing industry than with less information. Less information may lead to too much or too little capital. More complete information in the growing industry would allow live poultry dealers to send price signals to growers about levels of capital they desire. For example, if a live poultry dealer desires its birds be grown with a more capital-intensive housing type, it can increase its base payment rate in a grower ranking system for that particular housing type and provide projection sheets to growers so they can assess whether to upgrade. Live poultry dealers would have to increase the base compensation to a high enough level to spur the additional capital investment in upgrades. Similarly, too little compensation may result in under investment in capital, which is also inefficient.

Proposed § 201.214(b) would encourage live poultry dealers to supply inputs of more consistent quantity and quality to all growers. Thus, inferior chicks, which are more costly to grow, would likely be distributed more uniformly across growers. This would facilitate a level playing field and foster fair competition in poultry grower ranking systems. If proposed § 201.214 is finalized and becomes effective, growers would be compensated for their performance based more accurately on their skill and less so on the quality of inputs provided. The more efficient growers would receive more compensation in poultry grower ranking systems, which sends a signal to expand their offering of growing services. Less efficient growers would earn less, which sends a signal to reduce their offering of growing services or, at the extreme, to exit the industry. The result is lower costs to the industry as poultry grower ranking systems would incentivize the more efficient growers to expand and less efficient growers to contract or exit the industry.

Proposed § 201.214(c) would also provide a similar benefit to the industry. Under this section, the Secretary may consider whether a live poultry dealer includes poultry growers provided with dissimilar production variables in the ranking group in a manner that affects a poultry grower's compensation. The live poultry dealer would be expected to assure that growers are treated consistently as compared to other growers in the settlement group. This would allow growers to compete in poultry grower ranking systems on their skill level and not be disadvantaged by factors outside of their control. The result, again, is lower costs to the industry as the poultry grower ranking system would likely incentivize the more efficient growers to expand and the less efficient growers to reduce operations or exit the industry.

Proposed § 201.214(d) would benefit the industry by allowing the Secretary to consider whether a live poultry dealer has demonstrated a legitimate business justification for use of a poultry grower ranking system that would otherwise violate the P&S Act. This is a benefit for live poultry dealers as it provides a level of protection against potentially frivolous litigation.

Another important qualitative benefit of proposed § 201.214 is the increased ability for the enforcement of the P&S Act for use of poultry grower ranking systems in a manner that does not result in a harm or likelihood of harm to competition. This occurs through § 201.3(a), which states that conduct can be found to violate sections 202(a) and/or 202(b) of the P&S Act without a finding of harm or likely harm to competition and more specifically through § 201.210(b)(10) which clarifies that absent demonstration of a legitimate business justification, failing to use a poultry grower ranking system in a fair manner after applying the criteria in § 201.214 is unfair, unjustly discriminatory, or deceptive and a violation of section 202(a) of the P&S Act regardless of whether it harms or is likely to harm competition.

A simple example is a live poultry dealer consistently supplying inferior chicks to a particular grower. The grower is harmed by this conduct because the grower consistently under-performs in the poultry grower ranking system and receives lower compensation than if the grower had been provided higher quality chicks. This can be considered an unfair and deceptive practice under section 202(a) and/or as subjecting the grower to an unfair disadvantage under section 202(b). The impact of this harm to the grower is very small when compared to the entire industry and there is no harm to competition from this one instance. Because there is no harm or likely harm to competition, courts have been reluctant to find a violation of section 202(a) or (b) of the P&S Act in such a situation, despite the harm suffered by the individual poultry grower.

However, if similar, though unrelated, harm is experienced by a large number of growers, the cumulative effect does result in a harm to competition. The individual harm is inconsequential to the industry, but the sum total of all individual harm has the potential to be quite significant when compared to the industry and therefore, courts have found harm or likely harm to competition in such a situation. The regulations in this proposed rule, in conjunction with § 201.3(a), clarify that consistently supplying inferior chicks, absent demonstration of a legitimate business justification, would constitute unfair, unjustly discriminatory, or deceptive practices or devices under section 202(a) of the P&S Act or the giving of an undue or unreasonable preference, advantage, prejudice or disadvantage under section 202(b) of the P&S Act.

The sum of all individual harm is likely to increase total industry costs of producing poultry due to an inefficient allocation of resources. The cost of all unfair, unjustly discriminatory, or deceptive practices, or undue or unreasonable preferences or advantages to any poultry grower or undue or unreasonable prejudices or disadvantages are reflected in higher costs of producing poultry, with some portion of these costs passed along to consumers in the form of higher prices.

GIPSA expects proposed § 201.214 coupled with §§ 201.3(a) and 201.210(b)(10) to increase enforcement actions against live poultry dealers for use of poultry grower ranking systems in a manner that violates sections 202(a) and/or 202(b) when the use of the poultry grower ranking system does not harm or is not likely to harm to competition. Several appellate courts have disagreed with USDA's interpretation of the P&S Act that harm or likely harm to competition is not necessary in all instances to prove a violation of sections 202(a) or 202(b). In some cases in which the United States was not a party, these courts have concluded that plaintiffs could not prove their claims under section 202(a) and/or (b) without proving harm to competition or likely harm to competition. One reason the courts gave for declining to defer to USDA's interpretation of the statute is that USDA had not previously formalized its interpretation in a regulation.

Section 201.3 addresses that issue and §§ 201.214 and 201.210(b)(10) provide clarity regarding the circumstances under which use of a poultry grower ranking system, absent demonstration of a legitimate business justification, would constitute an unfair, unjustly discriminatory, or deceptive practice or device under section 202(a) of the P&S Act or the giving of an undue or unreasonable preference, advantage, prejudice or disadvantage under section 202(b) of the P&S Act. GIPSA expects the result would be additional enforcement actions successfully litigated, which will serve as a deterrent to using a poultry grower ranking system in a manner that violates sections 202(a) or (b) of the P&S Act. Successful deterrence would likely result in lower overall costs throughout the entire production and marketing complex of all poultry and chicken.

Benefits to the industry and the market also arise from establishing parity of negotiating power between live poultry dealers and poultry growers by reducing the ability to abuse market power with the resulting deadweight losses.[39] Establishing parity of negotiating power in contracts promotes fairness and equity and is consistent with GIPSA's mission ''[T]o protect fair trade practices, financial integrity, and competitive markets for livestock, meats and poultry.'' [40]

Regulatory Alternative 2: Cost-Benefit Summary of the Preferred Alternative

GIPSA expects the annualized costs of § 201.214 will be $3.77 million at a three percent discount rate and $4.18 million at a seven percent discount rate. GIPSA was unable to quantify the benefits of the regulations, but explained numerous qualitative benefits derived from increased information and reduced information asymmetries. The regulation contains several provisions that GIPSA expects will: (1) Improve efficiencies in the formation of capital in the poultry growing industry; and (2) lower costs to the industry as grower ranking systems will incentivize the more efficient growers to expand and less efficient growers to reduce operations or exit the industry. Another benefit of proposed § 201.214 is the deterrent effect of increased enforcement of the P&S Act for violations of section 202(a) or (b). This, in turn, would reduce instances of unfair, unjustly discriminatory, or deceptive practices or devices and undue or unreasonable preferences, advantages, prejudices, or disadvantages and increased efficiencies in the marketplace. At the same time, allowing the Secretary to consider legitimate business justifications for use of a poultry grower ranking system in a manner that might otherwise be seen as a violation of section 202(a) or (b) of the P&S Act would provide a level of protection against potentially frivolous litigation. Thus, proposed § 201.214 would likely increase efficiency, lower costs, and reduce market failures in the poultry industry. These benefits would accrue to all segments of the poultry value chain, and ultimately consumers.

Regulatory Alternative 3: Contract Duration—Phased Implementation

GIPSA considered a third regulatory alternative of phased implementation. Under this third alternative, proposed § 201.214 would only apply to poultry growing contracts when they expire, are altered, or new contracts are put in place. Consider for example, a poultry growing contract with 3 years remaining in the contract when the regulations become effective. Proposed § 201.214 would not be applicable to this contract, under phased implementation, until the contract expires after 3 years and is either modified or replaced.

Regulatory Alternative 3: Cost Estimation of Phased Implementation

GIPSA estimated the costs of phased implementation by multiplying the majority of the ten-year total costs of the preferred alternative (Table 7) for each year of the first 10 years the rule would be in effect by the percentage of contracts expiring or altered in the same year. The data on contract lengths for broiler production appear in the table below.

TABLE 10—PRODUCTION AND MARKETING CONTRACT DURATIONS

Contract duration	Broiler production [41] (%)
Short Term < = 12 months ...	65.20
Medium Term 13–60 months	19.20
Long Term > 60 months	15.60

The data in the table above show that 65.2 percent of broiler production contracts have a duration of 12 months or less and 84.4 percent have a duration of 60 months or less. Only 15.64 percent of broiler production contracts are longer than 60 months in duration.

For the first year of the regulation, GIPSA multiplied the costs of § 201.214 by 65.20 percent. The one exception is the cost of the development of CMSs. GIPSA's experience reviewing poultry growing contracts suggests that most live poultry dealers have some contracts that are of a short-term duration. Therefore, GIPSA estimates that all live poultry dealers would have to develop a CMS in the first year after the implementation of the regulation. GIPSA allocates 100 percent of CMS development costs in the first year under the phased implementation alternative. All other direct administrative costs are multiplied by 65.20 percent in the first year.

For years 2 through 5, GIPSA followed the same procedure and adjusted total industry costs by 84.4 percent, the number of contracts that are 5 years or less in duration. For years 6 through 10, GIPSA applied 100 percent of the preferred alternative costs to reflect the full phase in of costs.

The following tables show the 10-year total costs of the phased implementation alternative. The 10-year total costs for each year of the preferred alternative (Table 7) are also shown for convenience.

TABLE 11—PHASED IMPLEMENTATION TOTAL COSTS OF § 201.214

Year	Preferred alternative ($ millions)	Phased implementation ($ millions)
2018	17.37	13.23
2019	3.47	2.93
2020	3.47	2.93
2021	3.47	2.93
2022	3.47	2.93
2023	1.74	1.74
2024	0.87	0.87
2025	0.43	0.43
2026	0.22	0.22

[39] MacDonald, J. and N. Key. ''Market Power in Poultry Production Contracting? Evidence from a Farm Survey.'' *Journal of Agricultural and Applied Economics.* 44(4) (November 2012): 477–490. Discusses evidence for the effect of concentration on grower compensation.

[40] See additional discussion in Steven Y. Wu and James MacDonald (2015) ''Economics of Agricultural Contract Grower Protection Legislation,'' *Choices* 30(3): 1–6.

[41] USDA's Economic Research Service Agricultural Resource Management Survey (ARMS) 2011.

TABLE 11—PHASED IMPLEMENTATION TOTAL COSTS OF § 201.214—Continued

Year	Preferred alternative ($ millions)	Phased implementation ($ millions)
2027	0.11	0.11
Totals	34.64	28.32

GIPSA estimates that the first-year total costs of § 201.214 under the phased implementation alternative would be $13.23 million and the 10-year total costs would be $28.32 million. As the table shows, the costs in the first 5 years are lower under the phased implementation option than under the preferred alternative because regulated entities with contracts longer than 1 year are not covered until the contracts expire, are modified, or replaced.

Regulatory Alternative 3: NPV of 10-Year Total Costs of Phased Implementation

GIPSA calculated the NPV of the 10-year total costs of proposed § 201.214 under phased implementation using both a three percent and seven percent discount rate as required by Circular A–4. The NPVs are shown in the following table.

TABLE 12—NPVS OF TEN-YEAR TOTAL COSTS OF PROPOSED § 201.214—PHASED IMPLEMENTATION

Discount rate	($ millions)
3 Percent	26.18
7 Percent	23.77

GIPSA expects the NPV of the 10-year total costs of § 201.214 under the phased implementation option to be $26.18 million at a three percent discount rate and $23.77 million at a seven percent discount rate.

Regulatory Alternative 3: Annualized Costs of Phased Implementation

GIPSA then annualized the costs of § 201.214 using both a three percent and seven percent discount rate as required by Circular A–4 and the results appear in the following table.

TABLE 13—ANNUALIZED COSTS OF PROPOSED § 201.214—PHASED IMPLEMENTATION

Discount rate	($ millions)
3 Percent	3.07
7 Percent	3.38

GIPSA expects the annualized costs of § 201.214 under the phased implementation option to be $3.07 million at a three percent discount rate and $3.38 million at a seven percent discount rate.

Regulatory Alternative 3: Benefits of the Phased Implementation Alternative

The benefits of phased implementation are identical to the benefits of the preferred alternative with the exception of when the benefits will be received and the amount of the benefits. Like the costs, the benefits will be received only when contracts expire, are modified, or new contracts are put in place. Moreover, benefits to be received in the future are worth less than benefits received today. The benefits will be received in the same proportion of the total costs and are based on contract durations. The benefits of phased implementation are less than under the preferred alternative because the full benefits will not be received until all contracts have expired, been modified, or replaced by new contracts. The full benefits of phased implementation will be received beginning in year 6.

Regulatory Alternative 3: Cost-Benefit Summary of Phased Implementation

GIPSA expects the annualized costs of § 201.214 under the phased implementation option to be $3.07 million at a three percent discount rate and $3.38 million at a seven percent discount rate. The benefits will be received in the same proportion as total costs and are based on contract durations. The benefits of the phased implementation alternative are less than under the preferred alternative because the full benefits will not be received until all contracts have expired, been altered, or replaced by new contracts.

Cost-Benefit Comparison of Regulatory Alternatives

The status quo alternative has zero marginal costs and benefits as GIPSA does not expect any changes in the industry. GIPSA compared the annualized costs of the preferred alternative to the annualized costs of the phased implementation alternative by subtracting the annualized costs of phased implementation from the preferred alternative and the results appear in the following table.

TABLE 14—DIFFERENCE IN ANNUALIZED COSTS OF PROPOSED § 201.214 BETWEEN THE PREFERRED ALTERNATIVE AND THE PHASED IMPLEMENTATION ALTERNATIVE

Discount rate	($ millions)
3 Percent	0.70
7 Percent	0.80

The annualized costs of the phased implementation alternative is $0.70 million less expensive using a three percent discount rate and $0.80 million less expensive using a seven percent discount rate. As is the case with costs, the benefits of the preferred alternative will be highest for the preferred alternative because the full benefits will be received immediately and not when contracts have expired, been altered, or replaced by new contracts as is the case under the phased implementation alternative.

Though the phased implementation alternative would save between $0.70 million and $0.80 million on an annualized basis, this alternative would deny the protections offered by proposed § 201.214 to a substantial percentage of poultry growers for five or more years based on the length of their production contracts. As the data in Table 10 show, 15.6 percent of poultry growers have contracts with durations exceeding five years. Under the phased implementation alternative, these growers would continue to be exposed to the potential market failures discussed above until their contracts expire or are renewed. GIPSA considered all three regulatory alternatives and believes that the preferred alternative is the best alternative as the benefits of the regulation will be captured immediately by all growers, regardless of the length of their contracts.

Regulatory Flexibility Analysis

The Small Business Administration (SBA) defines small businesses by their North American Industry Classification System Codes (NAICS).[42] Live poultry dealers, NAICS 311615, are considered small businesses if they have fewer than 1,250 employees. Broiler and turkey producers, NAICS 112320 and 112330, are considered small businesses if their sales are less than $750,000 per year.

GIPSA maintains data on live poultry dealers from the annual reports these firms file with GIPSA. Currently, there are 133 live poultry dealers that would be subject to the proposed regulations. According to U.S. Census data on County Business Patterns, there were 74 poultry slaughter firms that had more than 1,000 employees in 2013.[43] The difference yields approximately 59 poultry slaughters that have fewer than 1,000 employees and would be considered small businesses that would be subject to the proposed regulations.

Another factor, however, that is important in determining the economic effect of the regulations is the number of contracts held by a firm. GIPSA records for 2014 indicated there were 21,925 poultry production contracts in effect, of which 13,370, or 61 percent, were held by the largest six live poultry dealers, and 90 percent (19,673) were held by the largest 25 live poultry dealers. These 25 live poultry dealers are all in the large business SBA category, whereas the 21,925 poultry growers holding the other end of the contracts are almost all small businesses by SBA's definitions.

To the extent the proposed rule imposes costs, these costs are expected to be borne by live poultry dealers. The costs likely include legal review of contracts, record-keeping, administrative costs, developing a CMS, and developing projection sheets.

Live poultry dealers classified as large businesses are responsible for about 89.7 percent of the poultry growing contracts. Assuming that live poultry dealers classified as small businesses will bear about 10.3 percent of the costs, expected costs in the first year for live poultry dealers classified as small businesses would be $1.8 million.[44] Expected 10-year costs annualized at a three percent discount rate for live poultry dealers classified as small businesses would be $387,000. Expected 10-year costs annualized at a seven percent discount rate for live poultry dealers classified as small businesses would be $429,000.

In considering the impact on small businesses, GIPSA considered the average costs and revenues of each small business impacted by § 201.214. The number of small businesses impacted by § 201.214, by NAICS code, as well as the per entity, first-year and annualized costs at both the three percent and seven percent discount rates appear in the following table.

TABLE 15—PER ENTITY COSTS TO SMALL BUSINESSES OF § 201.214

NAICS	Number of small business	First year ($)	Annualized costs—3% ($)	Annualized costs—7% ($)
311615—Poultry	59	30,246	6,563	7,278

The following table compares the average per entity first-year and annualized costs of § 201.214 to the average revenue per establishment for all firms in the same NAICS code. The annualized costs are slightly higher at the seven percent rate than at the three percent rate, so only the seven percent rate is shown as it is the higher annualized cost.

TABLE 16—COMPARISON OF PER ENTITY COST TO SMALL BUSINESSES OF § 201.214 TO REVENUES

NAICS	Number of small business	Average first-year cost per entity ($)	Average annualized cost per entity ($)	Average revenue per establishment ($)	First-year cost as percent of revenue (%)	Annualized cost as percent of revenue (%)
311615—Poultry	59	30,246	7,278	13,842,548	0.22	0.05

The revenue figure in the above table come from Census data for live poultry dealers, NAICS code 311615.[45]

As the results in Table 16 demonstrate, the first-year and annualized costs of § 201.214 as a percent of revenue is small at less than one percent.

Based on the above analyses regarding § 201.214, GIPSA certifies that this rule is not expected to have a significant economic impact on a substantial number of small business entities as defined in the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*). While confident in this certification, GIPSA acknowledges that individual businesses may have relevant data to supplement our analysis. We would encourage small stakeholders to submit any relevant data during the comment period.

Executive Order 12988

This proposed rule has been reviewed under Executive Order 12988, Civil Justice Reform. These actions are not intended to have retroactive effect, although in some instances they merely reiterate GIPSA's previous interpretation of the P&S Act. This proposed rule would not pre-empt state or local laws, regulations, or policies, unless they present an irreconcilable conflict with this rule. There are no

[42] See: *http://www.sba.gov/idc/groups/public/documents/sba_homepage/serv_sstd_tablepdf.pdf.* Accessed on August 26, 2016.

[43] *http://factfinder.census.gov/faces/tableservices/jsf/pages/productview.xhtml?src=bkmk.* Accessed on August 26, 2016. The U.S. Census data reports data in thousands making 1,000 the closest number of employees to SBA's small business classification of 1,250 employees.

[44] Estimated first year costs of $17.37 million × 10.27 percent of firms that are small businesses = $1.8 million.

[45] Source: *http://www.census.gov/data/tables/2012/econ/susb/2012-susb-annual.html.* Accessed on November 29, 2016.

administrative procedures that must be exhausted prior to any judicial challenge to the provisions of this proposed rule. Nothing in this proposed rule is intended to interfere with a person's right to enforce liability against any person subject to the P&S Act under authority granted in section 308 of the P&S Act.

Executive Order 13175

This proposed rule has been reviewed in accordance with the requirements of Executive Order 13175, ''Consultation and Coordination with Indian Tribal Governments.'' Executive Order 13175 requires Federal agencies to consult and coordinate with tribes on a government-to-government basis on policies that have tribal implications, including regulations, legislative comments or proposed legislation, and other policy statements or actions that have substantial direct effects on one or more Indian tribes, on the relationship between the Federal Government and Indian tribes or on the distribution of power and responsibilities between the Federal Government and Indian tribes.

GIPSA has assessed the impact of this rule on Indian tribes and determined that this rule does not, to our knowledge, have tribal implications that require tribal consultation under EO 13175. If a tribe requests consultation, GIPSA will work with the Office of Tribal Relations to ensure meaningful consultation is provided where changes, additions, and modifications identified herein are not expressly mandated by Congress.

Paperwork Reduction Act

This proposed rule does not contain new or amended information collection requirements subject to the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*). It does not involve collection of new or additional information by the federal government.

E-Government Act Compliance

GIPSA is committed to compliance with the E-Government Act, to promote the use of the Internet and other information technologies to provide increased opportunities for citizen access to Government information and services, and for other purposes.

List of Subjects in 9 CFR Part 201

Contracts, Poultry, Livestock, Trade Practices.

For the reasons set forth in the preamble, we propose to amend 9 CFR part 201 to read as follows:

PART 201—Regulations Under the Packers and Stockyards Act

■ 1. The authority citation for Part 201 continues to read as follows:

Authority: 7 U.S.C. 181–229c.

■ 2. Amend § 201.210 by adding paragraph (b)(10) to read as follows:

* * * * *

(b) * * *

(10) Failing to use a poultry grower ranking system in a fair manner after applying the criteria in § 201.214.

■ 2. Add new § 201.214 to read as follows:

§ 201.214 Poultry grower ranking systems.

The Secretary may consider various criteria when determining whether a live poultry dealer has engaged in a pattern or practice to use a poultry grower ranking system to compensate poultry growers in an unfair, unjustly discriminatory, or deceptive manner, or in a way that gives an undue or unreasonable preference or advantage to any poultry grower or subjects any poultry grower to an undue or unreasonable prejudice or disadvantage. These criteria include, but are not limited to:

(a) Whether a live poultry dealer provides sufficient information to enable a poultry grower to make informed business decisions. Such information should include the anticipated number of flocks per year, the average gross income from each flock, and any other information necessary to enable a poultry grower to calculate the expected income from the poultry growing arrangement;

(b) Whether a live poultry dealer supplies inputs of comparable quality and quantity to all poultry growers in the ranking group; and whether there is a pattern or practice of supplying inferior inputs to one or more poultry growers in the ranking group. Inputs include birds, feed, medication, and any other input supplied by the live poultry dealer;

(c) Whether a live poultry dealer includes poultry growers provided with dissimilar production variables in the ranking group in a manner that affects a poultry grower's compensation. Production variables include, but are not limited to, the density at which the live poultry dealer places birds, the target slaughter weights of the birds, and bird ages that vary by more than seven days; and

(d) Whether a live poultry dealer has demonstrated a legitimate business justification for use of a poultry grower ranking system that may otherwise be unfair, unjustly discriminatory, or deceptive or gives an undue or unreasonable preference or advantage to any poultry grower or subjects any poultry grower to an undue or unreasonable prejudice or disadvantage.

Larry Mitchell,

Administrator, Grain Inspection, Packers and Stockyards Administration.

[FR Doc. 2016–30429 Filed 12–19–16; 8:45 am]

BILLING CODE 3410–KD–P

DEPARTMENT OF TRANSPORTATION

Federal Aviation Administration

14 CFR Part 39

[Docket No. FAA–2016–9501; Directorate Identifier 2016–NM–137–AD]

RIN 2120–AA64

Airworthiness Directives; The Boeing Company Airplanes

AGENCY: Federal Aviation Administration (FAA), DOT.

ACTION: Notice of proposed rulemaking (NPRM).

SUMMARY: We propose to adopt a new airworthiness directive (AD) for The Boeing Company Model 777 airplanes. This proposed AD was prompted by reports of uncommanded altitude display changes in the mode control panel (MCP) altitude window. This proposed AD would require replacing the existing MCP with a new MCP having a different part number. We are proposing this AD to address the unsafe condition on these products.

DATES: We must receive comments on this proposed AD by February 3, 2017.

ADDRESSES: You may send comments, using the procedures found in 14 CFR 11.43 and 11.45, by any of the following methods:

- *Federal eRulemaking Portal:* Go to *http://www.regulations.gov.* Follow the instructions for submitting comments.
- *Fax:* 202–493–2251.
- *Mail:* U.S. Department of Transportation, Docket Operations, M–30, West Building Ground Floor, Room W12–140, 1200 New Jersey Avenue SE., Washington, DC 20590.
- *Hand Delivery:* Deliver to Mail address above between 9 a.m. and 5 p.m., Monday through Friday, except Federal holidays.

For service information identified in this NPRM, contact Boeing Commercial Airplanes, Attention: Data & Services Management, P.O. Box 3707, MC 2H–65, Seattle, WA 98124–2207; telephone: 206–544–5000, extension 1; fax: 206–766–5680; Internet: *https://www.myboeingfleet.com.* You may view