Date: December 29, 2009

To: Department of Justice and USDA

From: Robert C. Marshall, Professor of Economics, Penn State University
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Re: Justice Department and USDA Public Workshops To Explore Competition Issues in the Agriculture Industry

Public Disclosure:

Robert C. Marshall is a partner in the economics consulting firm Bates White, LLC.
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This memo is in response to the August 5, 2009, Department of Justice announcement of the "Justice Department and USDA Public Workshops To Explore Competition Issues in the Agriculture Industry."[1]

Implement Robust Auction Procedures

In the beef packing industry, packers purchase fed cattle through an auction process described in US v. JBS SA, CA No. 08-CV-5992, Amended Complaint (D. Ill 2008):[2]

"Packers purchase the majority of fed cattle on a weekly 'cash' or 'spot' market that is centered in the High Plains region. Over the course of the week, feedlots obtain bids from cattle buyers from several companies. Typically, after several days of a 'bid and quibble' process, most transactions clear within a period of a few hours late in the week. Throughout the 'bid and quibble' process, packers have extensive and timely information about the cash market. Packers regularly obtain detailed information regarding competitive bids, sales quantities, and prices from feedlot managers. In addition, packers have access to pricing and volume information from numerous commercial and governmental sources, including aggregated but detailed information reported daily by the USDA. Packers also purchase fed cattle under 'grid' or 'formula' pricing arrangements and forward contracts. The applicable base price under these pricing arrangements is often linked to one of several USDA-reported regional cash prices. Grids typically include discounts or premiums that are based on the characteristics of the cattle carcasses." (paragraphs 19-21)

If coordination among buyers is a concern, then we propose that sellers, with the support of the USDA, should implement an auction procedure that is substantially more robust to coordination.

To this end, we recommend that for agricultural markets where coordination among large buyers is a concern, the USDA should implement the Federal Communication Commission's spectrum license auction procedures for the sale of the agricultural commodity. The FCC's auction

[1] http://www.justice.gov/atr/public/press_releases/2009/248797.htm
[2] http://www.justice.gov/atr/cases/f239500/239578.htm

procedures are fully automated, well-tested, and designed for the sale of large numbers of geographically dispersed lots to a concentrated set of buyers. Just as a particular spectrum license is characterized by its location and spectrum characteristics, so would a lot of fed cattle be characterized by its location and characteristics. The FCC's procedures facilitate the aggregation by buyers of their desired mix of inputs, including potentially inputs available in multiple specific geographic areas.

The FCC's procedures have been adapted over time to facilitate large, recurring sales, while addressing concerns about coordination in bidding among large wireless service providers. Critical auction components include eligibility requirements, activity rules, anti-collusion rules, and anonymous bidding. The Economics Literature provides analysis supporting the role these procedures in deterring coordination among bidders.[3]

[3] See Robert C. Marshall and Leslie M. Marx (2009), "The Vulnerability of Auctions to Bidder Collusion," *Quarterly Journal of Economics* 124(2), 883-910 (showing the role of anonymous bidding procedures in deterring collusion); Leslie M. Marx (2006), "Economics at the Federal Communications Commission," *Review of Industrial Organization* 29, 349-368 (discussing the FCC's decision to implement anonymous bidding in spectrum license auctions); and William E. Kovacic, Robert C. Marshall, Leslie M. Marx, and Matthew E. Raiff (2006), "Bidding Rings and the Design of Anti-Collusion Measures for Auctions and Procurements," in *Handbook of Procurement*, edited by N. Dimitri, G. Piga and G. Spagnolo, Cambridge University Press, Chapter 15, 381-411 (discussing auction and procurement procedures that reduce vulnerability to collusion).