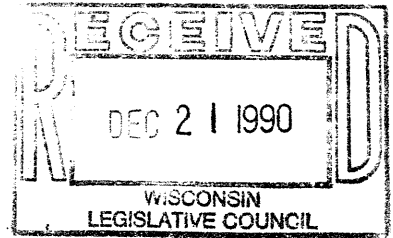


Date: April 11, 1988

To: Kevin J. O'Connor
Assistant Attorney General
Unit Head
Consumer Protection and Antitrust Unit

File - APD



From: Matthew J. Frank *MF*
Assistant Attorney General

Subject: Conclusion of National Cheese Exchange Investigation

I. Background

On November 20, 1987, the Wisconsin Assembly passed 1987 Assembly Resolution 6, which requested the attorney general to investigate the decline of cheese prices on the National Cheese Exchange (NCE) last fall. The Assembly requested the attorney general "to investigate the cause of recent price declines on the National Cheese Exchange and to prosecute any violation of law found to have occurred." The resolution also refers to rumors of "market manipulation, in the form of collusion, price-fixing, conspiracy or other illegal activities in restraint of trade." Prior to the passage of the Assembly resolution, the attorney general had received similar requests for an investigation from Representatives Mary Hubler, Barbara Linton and Barbara Gronemus.

In response to these requests for an investigation, the attorney general referred the complaint to the Consumer Protection and Antitrust Unit to conduct a preliminary investigation to determine whether there was any evidence of price-fixing or collusion or other violations of law on the NCE. Investigator Rosemary Perrizo and I conducted the investigation.

II. Applicable Laws

The Wisconsin Department of Justice is given the authority to investigate and prosecute violations of Wisconsin's antitrust laws under sec. 133.17, Stats.

Section 133.03(1) provides as follows: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce is illegal." Price-fixing, bid-rigging, and market or customer allocation are per se violations

of the federal Sherman Act as well as Wisconsin's antitrust laws. State v. Waste Management of Wisconsin, Inc., 81 Wis. 2d 555 (1978).

The Legislature has provided for criminal penalties for violations of sec. 133.03(1). A person convicted of price-fixing or other similar restraints of trade may be imprisoned for up to five years, and may be fined \$50,000. A corporation may be fined up to \$100,000 for engaging in this unlawful activity. Sec. 133.03(1).

III. Investigation and Findings

Prior to conducting interviews of members of the NCE, we gathered background information on the NCE and the dairy industry. We interviewed representatives of the Wisconsin Department of Agriculture, as well as Truman Graf, Emeritus Professor of Agricultural Economics at the University of Wisconsin-Madison. (See Professor Graf's 1979 paper entitled "Thin Market Case Study--National Cheese Exchange," Exhibit 1 attached.)

We interviewed Attorney Richard J. Gould, president of the NCE, who pledged cooperation with the Department of Justice in its investigation. Mr. Gould supplied, and we reviewed the following: minutes of the meetings of the NCE board of directors for 1986 and 1987; current bylaws for and rules for trading on the NCE; a complete record of all trading activity on the NCE in 1986 and 1987; a list of all the companies which are members of the NCE; and a list of all of the authorized traders on the NCE.

We conducted interviews of representatives of twenty-one companies which are members of the NCE. The twenty-one companies included those companies which do the most trading on the NCE. We also interviewed representatives of companies which occasionally trade on the NCE, as well as representatives of companies which are members but which very seldom or never trade on the NCE. Representatives from the following businesses were contacted and interviewed: Armour Dairy Products Company, Monroe, Wisconsin; Associated Milk Producers, New Ulm, Minnesota; Atlas Warehouse and Cold Storage, Green Bay, Wisconsin; Beatrice Foods Cheese Company, New Berlin, Wisconsin; Bongards' Creameries, Bongards, Minnesota; Borden Foods, Plymouth, Wisconsin; Dairy State Brands, Inc., Monroe, Wisconsin; Edelweiss Cheese Company, Marshfield, Wisconsin; Frigo Cheese Corporation, Green Bay, Wisconsin; Green Bay Cheese Company, Green Bay, Wisconsin; Kraft, Inc., Northbrook, Illinois; Land O' Lakes,

Inc., Spencer, Wisconsin; The Marketing Association of America, Green Bay, Wisconsin; Mid-America Dairymen, Inc., Green Bay, Wisconsin; Monroe Cheese Corporation, Monroe, Wisconsin; Sargento Cheese Company, Plymouth, Wisconsin; Schreiber Foods, Inc., Green Bay, Wisconsin; Universal Foods Corporation, Milwaukee, Wisconsin; Weyauwega Milk Producers, Weyauwega, Wisconsin; Wohlt Cheese Corporation, Fremont, Wisconsin; and World Wide Sales, Plymouth, Wisconsin.

We interviewed representatives of the National Farm Organization, the Wisconsin Cheese Maker's Association, and other observers of the NCE. We also attended an actual session of trading on the NCE to observe firsthand the way in which trading on the NCE occurs. All of the individuals and companies we talked to cooperated voluntarily with the investigation.

In the course of the investigation we looked for evidence of any agreements between traders or companies to fix the price of cheese on the NCE. We looked for evidence that traders agreed upon the price of cheese in advance of a trading session, or that they agreed or conspired to drive the NCE cheese price down. We tried to determine whether any trader or company was ever asked not to buy cheese on the NCE, which would indicate a possible agreement or conspiracy to drive the NCE cheese price down.

With respect to all of the above avenues of investigation, we found no evidence of such agreements. Accordingly, we found no evidence which would warrant a prosecution for violation of sec. 133.03(1).

Decisions and actions which competitors arrive at independently do not violate state price-fixing laws. Price-fixing can only occur between two or more parties. While there are a considerable number of companies which are members of the NCE, and which regularly attend its trading sessions, it is a fair characterization to state that the largest volume of trading on the NCE is engaged in by only a handful of companies. However, we did not find evidence of an agreement between these companies or any other companies to fix the price of cheese on the NCE.

In the course of the investigation we also gathered a great deal of information regarding general market conditions in the cheese industry and dairy industry overall. Without summarizing that information here, suffice it to say that a number of industry observers believe that the price declines on the NCE were a product of general market conditions and supply and demand factors, including, but not limited to, cuts in government price

Kevin J. O'Connor
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supports, a relatively strong milk supply compared to cheese demand, the termination of the whole-herd buyout program, an increase in cheese inventories prior to the fall of 1987 in anticipation of a milk shortage which did not develop as expected, weak growth in cheese sales compared to supply, to name but a few factors. Without analyzing every theory which has been advanced, it is clear that there are a number of credible reasons which explain why the price of cheese declined on the NCE in the fall of 1987 and again in early 1988.

In the absence of evidence of a price-fixing agreement, and in the presence of reasonable explanations for the price declines because of general market conditions in the industry, the Department of Justice can take no further action at this time.

CONCLUSION

As I made it clear at the beginning of this memo, the scope of our investigation was limited to the authority of the Department of Justice to investigate price-fixing and similar antitrust law violations. We did not, for example, analyze the effectiveness of the 1985 farm bill or the whole-herd buyout program, or whether a milk supply management program could alleviate the hardships on farmers, cheese manufacturers and other members of the dairy industry generally. These are matters not for antitrust law enforcement, but for Congress.

For these reasons, the investigation should be closed.

MJF:slp/X0617

Attachment

UW-Madison economists hope to finish report by summer's end

Madison

When the state Justice Department concluded in 1988 there was no evidence of price fixing on the National Cheese Exchange in Green Bay, it took a year to reach the decision.

Round two is another story.

A second investigation into the same matter began in 1991 and the Justice Department gave the chore to the Department of Agriculture, Trade and Consumer Protection. A decision on the investigation is expected sometime this summer, according to Bruce Marion, a University of Wisconsin-Madison ag economist who was asked to assist with the

process.

Mr. Marion and Willard Mueller, another UW-Madison ag economist, helped sort through endless trading information supplied by exchange members. Mr. Marion said that information at times was difficult to attain.

"When we started, it was hoped to have it completed in two years," Mr. Marion said. "But the date kept moving."

The main hurdle has been access to trading information. "A lot of parties have not been very cooperative," he said. "Some grudgingly cooperated. It has been like pulling teeth in some cases. We received information from all the members except one company (which he did not disclose) and that may

end up in court, but that is up to DATCP."

Reed Clopp, a DATCP attorney involved with the investigation, said the process has "pushed ahead as information comes in. You don't want to be in a situation where you miss something." He would not speculate on a conclusion, but said "a final report will indicate what happens after the investigation, but it is too soon to say if anything is being done wrong."

Mr. Marion said the National Cheese Exchange is a rare institution.

"It is unique," he said. "They represent a small amount of total cheese sales, but have a big market impact."

—Bob Kliebenstein

Farmers question cheese exchange investigation

Mount Horeb

June 1 was an ideal day for farmers to be in the field finishing up corn planting or cutting hay.

But a group of southwest Wisconsin farmers chose to forego fieldwork for the morning to address something they deem more important.

Five farmers along with Denny Caneff, outgoing executive director of the Wisconsin Rural Development Center, met at Dennis Jelle's farm to discuss the Department of Agriculture, Trade and Consumer Protection's investigation into trading practices on the National Cheese Exchange in Green Bay.

The group agreed the process is taking too long and meanwhile, Wisconsin continues losing dairy farms.

The investigation, the second of its kind, began in 1991 when milk prices plummeted after peaking due to the 1988 drought. Milk peaked around \$16 per hundred during the summer of 1989 and plunged to \$11 by 1990. Mr. Caneff said the drop suggested possible collusion

among exchange members in cheese pricing.

Mr. Jelle said a similar investigation took place in 1987 by the state Justice Department. After a year, investigators found no evidence exchange members plotted to manipulate cheese prices. Mr. Jelle said many of the main players on the exchange in 1995 are the same as 1987.

The first investigation was conducted improperly, Mr. Jelle said.

"They (exchange members) knew about the investigation and had time to clean up their act," he said. "They had three months' notice. It should have been done like a criminal case. You have to catch two buyers talking about lowering prices over the phone and that is pretty hard to do."

The producers contend companies like Kraft and Beatrice Foods drive cheese prices down in order to buy cheap cheese. That leaves dairy farmers sitting on the outside regarding milk price, they said. When large corporations have enough cheese, milk prices inch slightly upward until they need to buy again and the cycle continues, they added.

The second investigation, which began in 1991, was turned over to DATCP. Mr. Jelle said the switch was to lull farmers into thinking the investigation would have more clout in the ag community.

"It was done to pacify farmers," he said.

Jim McGhec, a Hollandale farmer, said turning the investigation over to DATCP buried it deeper in bureaucracy. "Laws are being written by the people who are working against the farmer," he said.

While the investigation continues, Keith Wilson, a Cuba City farmer, said producers continue vanishing, victims of economic uncertainty. "A penny drop in the exchange means a 10-cent drop in milk prices," he said. Mr. Wilson said dairy producers must be aware of disturbing trends.

"The trend is to privatize everything, even in government. That is OK," he said. "But in dairy we are facing what is already happening in the meat industry. You have a few companies controlling the cheese exchange."

Belmont farmer Art Wedig holds little faith in the investiga-

tion after hearing a comment from Wisconsin Secretary of Agriculture Alan Tracy.

"Mr. Tracy told farmers what goes on in the exchange is an in-house problem and they can police themselves," Mr. Wedig said.

Mr. Caneff was blunt in his perception of investigation results.

"The outcome of the investigation will be shaped by people who are big contributors to (Gov.) Tommy Thompson," he said. "The great paradox here is a company like Kraft does not even make cheese, but they sell it."

Mr. Caneff said heat was turned up on the investigation in April when DATCP refused an open records request from WRDC and the Fond du Lac Congregations United and Strong, or FOCUS, about information on the investigation. They were refused because the information is part of an ongoing investigation, he added.

"I think DATCP has been asleep at the wheel," Mr. Caneff said. "Let's get some answers to this and get the exchange cleaned up."

—Bob Kliebenstein

DATCP should deliver results on cheese exchange probe

To the Editor:

Here is a quiz in honor of June Dairy Month: Which of the following has been dragged out for the last 38 months without a resolution?

Possible answers include: (a) the O.J. Simpson murder trial; (b) the major league baseball strike; (c) the war in Bosnia; (d) the investigation of trading at the National Cheese Exchange in Green Bay by the Wisconsin Department of Agriculture, Trade and Consumer Protection.

The correct answer, (d), is the least well-covered by most media, but arguably the most important to Wisconsin and other dairy regions. Our state's cornerstone \$2.96 billion dairy industry has lost hundreds of millions of dollars over a matter of months when trading activities on the cheese exchange by dairy marketing giants such as Kraft/Phillip Morris and Pizza Hut/Pepeico have sent milk and cheese prices plummeting.

After the steepest such plunge, during late 1991, Gov. Thompson pledged that a full-scale, no-holds-barred investigation of trad-

ing at the unregulated exchange would be conducted. A team of experts from UW-Madison, including research faculty with expertise in ag economics, food systems and antitrust law, was commissioned by DATCP Secretary Alan Tracy in February 1992 to find out whether the Green Bay exchange is being used to inflate some firms' profits to the detriment of dairy producers, cheesemakers and our rural economy.

During the investigation, which was supposed to take about one year, DATCP's job was to expedite data collection from the cheese companies and dairy cooperatives trading on the NCE. DATCP has subpoena power to do this, unlike the professors. By late 1992, Secretary Tracy was saying that the investigation might take another year. At the end of 1993, no end was in sight. Mr. Tracy's people indicated that some of the 20 trading entities from whom data was requested were unwilling to provide info.

Yet DATCP appeared reluctant to use its subpoena power, and seemed at least partially resposi-

ble for delaying any vigorous prosecution of the investigation.

Secretary Tracy and Secretary of Administration James Klausner both blamed a handful of cheese companies for refusing to cooperate in the investigation, but neither official would name the firms.

Former Tracy aide Will Hughes told impatient Sheboyan County farmers in the spring of 1994 that he would return by fall with the completed investigation. Three weeks later Mr. Hughes resigned from DATCP. Secretary Tracy himself has been fuzzy about the actual time frame for the study, telling a Green Bay paper last May that the investigation "had taken about a year and should be wrapped up by late 1994."

Mr. Tracy repeated this pledge to angry NFO and Farm Bureau dairy producers in an October 1994 session at Johnsonville facilitated by Republican State Assemblyman Cliff Ott. Then 1994 came and went, with lower prices, fewer farmers but still no concluded study.

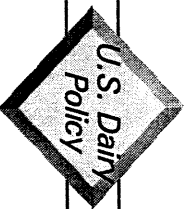
Since the Thompson administration took office, we have lost more than 8,000 dairy farms.

Cheesemakers are also shutting down, or being moved to California, Kentucky or New Mexico. Since DATCP started its "no-holds-barred" investigation, Wisconsin has twice been surpassed by California as the nation's No. 1 milk producer.

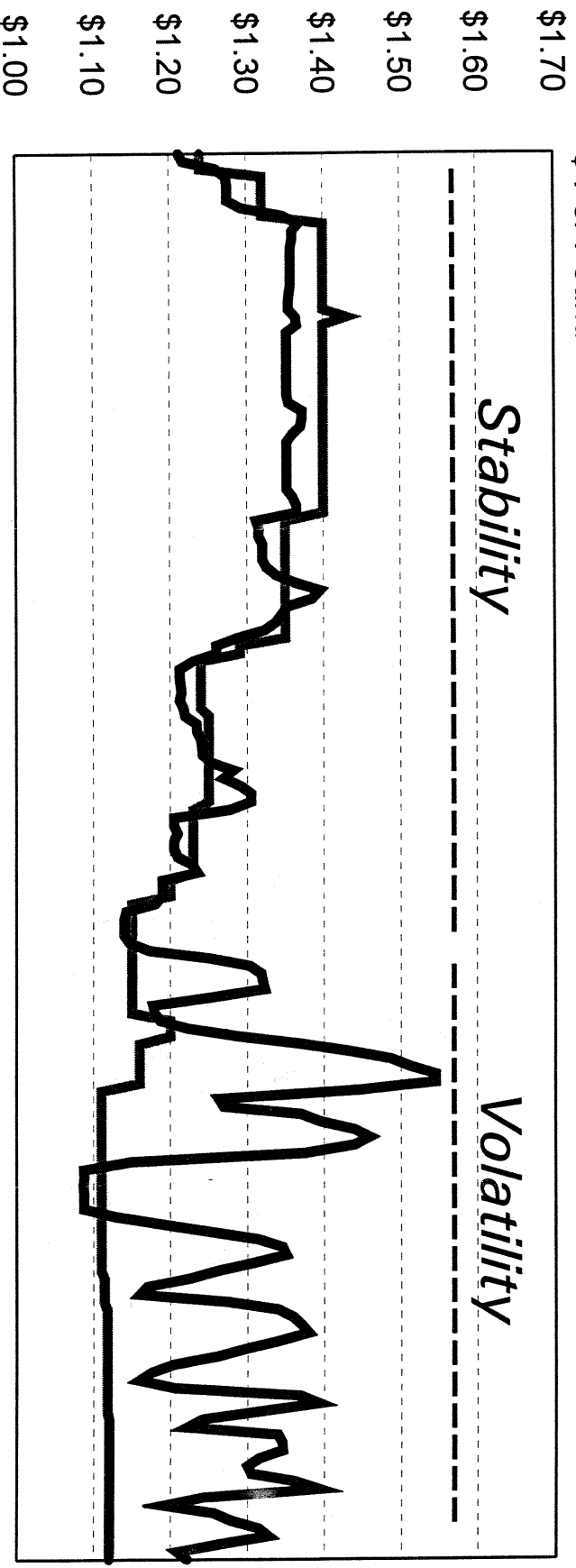
The viability of Wisconsin's most crucial economic sector — dairy — is directly tied to the weekly trading activity and pricing "opinions" of the Green Bay Cheese Exchange. We cannot afford to ignore either the importance or the suspiciousness of activities at the NCE which may be doing irreparable damage to America's Dairyland, rural incomes and farmers' spirits.

The Thompson administration has one last chance to demonstrate that it can provide a semblance of leadership by delivering its long-delayed investigation during June Dairy Month ... and by following up on the pertinent conclusions of the study. If Gov. Thompson, Secretary Tracy, Secretary Klausner, et al fail, the word should be spread far and wide, not only throughout Wisconsin, but in Iowa and New Hampshire as well.

Jay Klemmurd,
Sheboyan



A change in policy direction and budget pressures led to a gradual reduction in government intervention in the late 1980's.



- The support price level and mechanisms to implement the support price are set by Congress every five years. The USDA administers changes according to these provisions.
- The current price level was set by the 1990 Farm Bill, the 1995 Farm Bill will establish a support price for 1996-2000.

KRAFT GENERAL FOODS
KRAFT USA

SETH A. EISNER
VICE PRESIDENT
CHIEF COUNSEL

June 16, 1995

*ARM - File for
reference on
Cheese Exchange Budget
ARM*

Representative Alvin Ott
P.O. Box 8953
Madison, WI 53708

Dear Representative Ott:

Thanks for making some time to meet with Pete Christiansen and me on Tuesday, particularly at this very busy time of the year for you.

I am enclosing a copy of a letter that we distributed broadly throughout the dairy industry early in 1993. I hope you find it informative. If you are interested, it would be my pleasure to provide additional information about any of the subjects we discussed.

I checked into our purchases of cheese and other dairy products in the general vicinity of the Third District. We purchase various types of cheeses from AMPI/Morning Glory in Appleton, Stella in Fon du Lac, Weyauwega Cheese Company in Weyauwega, and -- a bit further away -- Wisconsin Dairy State in Rudolph. We purchase other dairy products such as cream, buttermilk and condensed milk from Galloway Cheese in Neenah, Level Valley in West Bend, Kemps-Marigold in Cedarburg and, again, Weyauwega Cheese in Weyauwega.

Once again, many thanks for your time.

Very truly yours,

Seth A. Eisner



KRAFT GENERAL FOODS

KRAFT USA

JAMES M. KILTS
PRESIDENT
KRAFT USA

January 15, 1993

Last week the Milwaukee Sentinel published a series of articles about current issues in the dairy industry. Kraft applauds the Sentinel for devoting its attention to these issues because of their importance to Wisconsin and all parts of the dairy industry. However, Kraft's assessment of these issues differs in several respects from the Sentinel's reports. Because we care about your views, we want to share our perspective on these matters with you.

Kraft's Role in the Dairy Industry

Kraft is proud of its success in the dairy industry. For 90 years, we have served consumers with high quality products. We have worked hard to increase consumer demand for the dairy products that we market. We have introduced new products that appeal to rapidly changing consumer tastes, and have vigorously promoted new uses for established products. By strengthening consumer demand, Kraft believes that our suppliers, as well as our customers, have and will continue to benefit.

From time to time, we have noticed some confusion about Kraft's place in the marketing chain and about our pricing practices in recent years. For example, contrary to some reports, Kraft does not sell products directly to the consumer. Rather, Kraft sells primarily to grocery stores. Kraft prices products at the wholesale level. Grocery stores then set the retail prices that consumers pay.

Driven by competition, Kraft has priced its products reasonably and competitively. During the past five years, net prices of our products increased a total of 8%, reflecting not only higher commodity cheese costs, but also the costs for labor, energy, transportation and marketing, which have increased at more than twice the rate of commodity cheese. In fact, over the last 11 years, Kraft's prices have increased only 2% annually, even though the Consumer Price Index (CPI) increased annually an average of 4%, the food component of the CPI increased 3.6%, and the cheese component of the CPI increased 3.2%. Taken together, our wholesale price increases have been reasonable in light of our overall cost increases.



To satisfy consumer demand for our products, Kraft purchases dairy products that account for about 11% of the U.S. milk supply. This includes the approximately 19% of the cheese produced in the U.S. that we manufacture or procure. These are significant volumes, but they do not confer on Kraft any market dominance or ability to influence price. Like other agricultural commodities, supply and demand determine milk and cheese prices.

Milk and Cheese Prices

In recent years, the federal government has reduced support prices for dairy products by almost 25%. This trend was the result of two principal factors. First, previous dairy programs which held support prices at higher levels were thought by Washington to be too costly, particularly in light of growing federal budget deficits. Second, throughout the 1980s, Washington pursued policies that promoted increased reliance on "free markets" in the agricultural sector.

As the support price was lowered, prices for milk and other dairy commodities were increasingly exposed to the forces of supply and demand. For instance, in 1989, when demand was strong and supplies were tight, milk prices rose dramatically, 30% in six months. By contrast, in the spring of 1991, demand was weak and supplies were plentiful, and prices fell abruptly.

As with all commodities, many forces influence the supply and demand for milk and cheese. Weather has been important, as has been the cost of feed. Price levels have also been critical as high milk prices stimulated production and lower prices restricted it. Over the longer term, technology has had a major impact on dairy supplies as output per cow and the size of farming operations have steadily increased. Similarly, demand for cheese and other dairy products has been influenced by shifting consumer preferences, government purchases, export opportunities, and the retail prices of all dairy products and their alternatives. Kraft, of course, does not control these underlying forces of supply and demand.

With the reduction in support prices, these upturns and downturns have become more frequent and more pronounced than in the past. This volatility has been stressful to all parts of the dairy industry including farmers, processors, wholesalers and retailers.

For these reasons, Kraft has supported an increase in federal price supports for dairy products.

Kraft's Relationship with its Suppliers

Kraft operates several plants that convert milk into bulk cheese and other plants that convert bulk cheese into packaged consumer products. Kraft does not make all of its own bulk cheese. We fill many of our requirements by purchasing bulk cheese from cooperatives and other cheese manufacturers. Kraft values our business relationships with both milk suppliers and bulk cheese suppliers.

Kraft buys milk from independent milk producers and cooperatives. Milk procurement is very competitive. Kraft is proud of the fact that we earn our producers' business every day of the year. Nothing binds our milk producers to Kraft other than a successful business relationship.

Kraft has longstanding relationships, many over 20 years, with most of our cheese suppliers. In most cases we buy the entire output of a plant. This works well for both parties. Producing plants are guaranteed an outlet and Kraft maintains the high quality standards that we need. We view our contract plants as partners. And this partnership, which includes technological cooperation, honoring commitments and paying our bills on time, has worked successfully for many years.

The National Cheese Exchange

The Sentinel articles describe at length and in colorful detail the National Cheese Exchange at Green Bay, Wisconsin.

Kraft, our suppliers and the rest of the industry have used the National Cheese Exchange (NCE) "opinion" as the basis for establishing bulk cheese prices for many years. The industry believes that the NCE provides a reasonable basis because bids, offers and trades there reflect supply and demand conditions for cheese.

The NCE has been in operation for more than 70 years. It has 40 members, representing buyers and sellers, including such manufacturers as ConAgra (Beatrice), Borden and Kraft, and large farmer cooperatives like MidAm, AMPI and Land O' Lakes. The Exchange, like other markets, provides a forum in which buyers and sellers can trade cheese.

There is widespread consensus among experts inside and outside of the industry that the NCE is an effective marketplace. The NCE allows participants to transact at prices which buyers are willing to bid and sellers are willing to offer.

A casual observer might be struck by the NCE's informal appearance. Instead of being housed in an imposing facility in one of the nation's financial centers, it meets in a modest, rented space in Green Bay, Wisconsin.

Some compare the NCE to futures markets for other commodities. But the National Cheese Exchange is not a futures market. It is a cash market. And, unlike many cash markets, the NCE pricing is public. The board is open for all to see who is buying and selling, and at what price.

Cash markets involve only those individuals willing to take physical possession of the commodity being traded. In the case of the NCE, this group of commercial participants includes cooperatives, processors, manufacturers and brokers. Most agricultural products have cash markets and they are generally unregulated because most market regulations are designed to protect casual "public" investors. There is no class of these "public" investors in cash markets generally, nor in the NCE specifically.

Kraft is open to any ideas that might improve the NCE. Ultimately, any changes in the Exchange would be a subject for all of its members, not just Kraft. And, given the dramatic changes in the dairy industry in recent years, we have welcomed industry discussions on improving market mechanisms.

Kraft's Trading on the NCE

Based on a review of publicly available information, the Sentinel pointed out that Kraft has participated in a significant portion of the transactions on the NCE in recent years. However, 70% of the sales we made in the last five years were in response to bids for cheese from other NCE members. That means Kraft was not initiating the transaction, nor establishing the price. We were merely selling cheese to another member at the price being bid by that member. Often the buyer was a farmer cooperative that decided what price to bid for cheese. Of all the weekly opinions on the Exchange in the past five years, 85% were established based on activity initiated by NCE members other than Kraft. Of those relatively few activities that resulted in a lower weekly opinion, 53% were initiated by NCE members other than Kraft.

In every respect, our trading practices have been based on sound business reasons. Our practices are entirely ethical and certainly legal.

Futures Markets

The contractual arrangements and the cash market used as the basis for pricing cheese have performed well in the past years. When prices were stable, these mechanisms were especially satisfactory. However, as the environment of relative price stability disappears, the industry should examine new mechanisms to manage price risks.

Indeed, changes in the past few years in the federal dairy policy have increased interest in broader markets for trading dairy product contracts, including cheese.

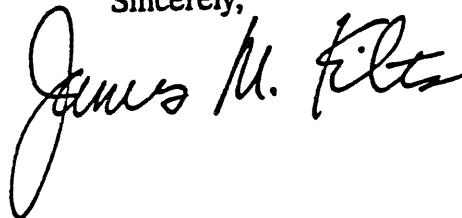
For example, the industry has introduced cash forward contracts for nonfat dry milk in recent years. More recently, there has been considerable interest in the development of futures markets for dairy products. In fact, a proposal to trade futures contracts for cheese and nonfat dry milk was approved by the board of directors of the Coffee, Sugar & Cocoa Exchange this week; it now goes before the Commodity Futures Trading Commission for review. If approved, trading in cheese and nonfat dry milk futures contracts could begin this summer.

Kraft welcomes and supports these efforts because we believe that these mechanisms provide the industry with another tool for managing price risk in volatile markets.

Conclusion

We hope that this discussion of these admittedly complex issues is helpful to your understanding of them. Thank you for allowing us to share Kraft's perspective.

Sincerely,

A handwritten signature in black ink that reads "James M. Filtz". The signature is written in a cursive style with a large, looping initial "J".

Embargoed for Tuesday, 3/19/96

NATIONAL CHEESE EXCHANGE INVESTIGATION

SUMMARY REMARKS

March 19, 1996

NATIONAL CHEESE EXCHANGE INVESTIGATION

SUMMARY REMARKS

The Wisconsin Department of Agriculture, Trade and Consumer Protection (DATCP) and the University of Wisconsin-Madison College of Agriculture and Life Sciences today announced the release of a major report on business practices related to bulk cheese pricing, including trading activities on the National Cheese Exchange. The report is the culmination of a comprehensive 3 ½ year investigation. The report examines the period 1980-1993, and focuses particularly on the years 1988-1993.

The investigation was jointly conducted by the Wisconsin Department of Agriculture, Trade and Consumer Protection and the Food System Research Group of the Department of Agricultural Economics, University of Wisconsin-Madison. The UW's Food System Research Group authored the report. The authors are Professors Willard F. Mueller and Bruce W. Marion and Research Scientists Dr. Maqbool Sial and Frederick Geithman, M.S.

The report raises serious concerns about the National Cheese Exchange (Exchange) as a mechanism for determining bulk cheese prices. Exchange prices affect all companies that buy and sell cheese. They also have a strong effect on milk prices paid to farmers.

REPORT CONTENTS

- Cheese is the most important manufactured dairy product in the U.S., commanding over 85 percent of Wisconsin milk and 33 percent of U.S. milk. Wisconsin produces approximately 30 percent of the nation's cheese, more than double California, the second ranking state. Manufacturers and marketers of cheese had sales of \$16 billion in 1992.
- The National Cheese Exchange, located in Green Bay, Wisconsin, is the only national cash auction market for bulk cheese. Members of the Exchange include major manufacturers, processors, marketers and brokers of cheese. Traders meet once each week for about 30 minutes to buy and sell cheddar cheese to each other in carload quantities (40,000 lb.). Cheese prices are established based on the last sale, highest bid or lowest offer made on the Exchange.
- During the period covered by the investigation, less than one-half of one percent of all cheese was sold on the Exchange. However, the Exchange has a major nationwide impact on bulk cheese prices. About 90 to 95 percent of all bulk cheese is sold under long-term cheese supply contracts in which the price is directly tied to the Exchange price. For example, a manufacturer may contract to supply cheese to a buyer at "4 cents over the Exchange" for the duration of the supply contract. Because "formula pricing" pegs cheese supply contracts to Exchange prices, the Exchange has a market impact that is far out of proportion to the amount of cheese traded there.

- Because cheese is the most important manufactured dairy product, cheese prices have a direct impact on milk prices paid to farmers. Exchange prices largely determine nationwide cheese prices and hence are directly linked to milk prices. Exchange prices are the major component in the “basic formula price” used in federal milk marketing orders.
- A significant shift in the trading patterns of leading Exchange traders occurred around 1988. During the period 1980-1987, companies that were predominantly sellers of bulk cheese off the Exchange also were predominantly sellers on the Exchange. Companies that were predominantly buyers of bulk cheese off the Exchange also were predominantly buyers on the Exchange. This pattern was reversed during 1988-1993, when several leading buyers off the Exchange became predominantly sellers on the Exchange and several of the leading sellers off the Exchange became predominantly buyers on the Exchange.
- This shift in trading patterns occurred at the same time that trading activity on the Exchange became more important in determining cheese prices. During 1980-1987, cheese prices were strongly influenced by the government dairy price support program. As support prices declined, cheese prices became more market driven. The volatility and range of cheese prices increased sharply during 1988-1993. In this environment, Exchange traders had both greater opportunity and greater incentive to influence cheese prices.
- Trading on the Exchange is concentrated among a handful of buyers and sellers. During the period 1988-1993, four companies accounted for 88 percent of all cheese sales on the Exchange. One company, Kraft General Foods, Inc., owned by Philip Morris Companies, Inc., accounted for 74 percent of all sales on the Exchange. Four companies accounted for 81 percent of all cheese purchases on the Exchange. Beatrice Cheese, Inc., owned by Con Agra, Inc., was the leading buyer, with 35 percent of all purchases on the Exchange.
- Cheese prices are broadly determined by national supply and demand. However, because of the small number of companies trading on the Exchange, and the disproportionate effect of Exchange trading on nationwide cheese and milk prices, individual companies may at times have the opportunity and incentive to use the Exchange to affect broader market prices to their advantage. This may distort overall market prices, so that they do not fairly reflect underlying market conditions.
- If a *buyer* of bulk cheese can reduce the Exchange price (and hence, prices in the overall market) by *selling* on the Exchange, the buyer may be able to reduce its overall cheese procurement costs. Similarly, if a *seller* of bulk cheese can increase the Exchange price (and hence, prices in the overall market) by *buying* on the Exchange, the seller may be able to increase its sales revenues in the overall market. The ability of individual Exchange traders to affect Exchange prices to their advantage depends on their relative market power.

- Kraft is the nation's largest cheese company, and the largest buyer of bulk cheese. Kraft purchases about 60 percent of its bulk cheese needs and manufactures the remainder. Kraft processes and packages cheese for sale primarily through retail food stores. During 1988-1992, about 45 percent of all cheese sold at retail had the Kraft brand name.
- Although Kraft is predominantly a buyer of bulk cheese off the Exchange, it was almost exclusively a seller on the Exchange during the period 1987-1993. This was a marked change from Kraft's trading activity during the period 1980-1986, when Kraft was both a leading buyer and seller on the Exchange (and bought over twice as much as it sold).
- Some companies that were major sellers of bulk cheese off the Exchange also changed their trading behavior, possibly in response to the changing behavior of Kraft and other traders. During the period 1980-1987, three leading sellers off the Exchange *sold* about 10 loads on the Exchange for every load they *bought* on the Exchange. But during the period 1988-1993, these manufacturers became primarily buyers on the Exchange, *buying* about 9 loads for every load they *sold*.
- An analysis of Kraft's trading activity from 1990 through 1992 suggests that at times Kraft sold on the Exchange at prices that were less than Kraft could have received off the Exchange. This raises the question whether companies may "trade against interest" on the Exchange in order to affect prices to their advantage in the larger cheese market. An in-depth analysis of Kraft's trading patterns also suggests that Kraft played a central role in shaping the pattern of prices over each price cycle during 1990-1992.
- The results of several statistical analyses were consistent with the above findings. One analysis suggests that, at times during 1988-1993, some traders influenced the level of prices on the Exchange. The analysis is consistent with the hypothesis that leading seller-traders, especially Kraft, had a significant negative impact on Exchange prices. The analysis did not find a statistically significant relationship between leading buyer-trader activity and Exchange prices.
- Based on their overall analysis, the authors conclude that the Exchange was not a reliable or accurate price discovery mechanism during the period 1988-1993. They also conclude that, as currently organized, the Exchange may facilitate market manipulation by individual firms. The authors emphasize, however, that they found no evidence of collusion between cheese companies.
- The authors emphasize that their analysis and conclusions are based on the years studied, 1988-1993. Insofar as the analysis reflects factors unique to these years, it may be an imperfect predictor of the future performance of the Exchange. For example, the apparent depression of bulk cheese prices during some of this period may not be sustainable in the future. This does not diminish the significance of the study findings or the need to either replace the Exchange or enhance its competitive performance.

REPORT IMPLICATIONS

The dairy industry, like other industries, needs an effective price discovery mechanism that can serve as a basis for pricing bulk cheese transactions. The goal for the industry should be to have efficient and competitive prices that accurately reflect underlying supply and demand conditions.

For many commodities, there is both a broad-based "cash" market and an active "futures" market that signals expectations about future supply and demand. Broad industry participation in these markets helps to ensure that the markets are representative of actual market conditions and expectations. Broad participation also reduces risks of price manipulation. This report calls into question whether prices on the Exchange fairly and accurately reflect national supply and demand conditions.

Until 1993, there was no "futures" market for cheese or milk. Although futures markets now exist, use of those markets has been limited to date. The effectiveness of the cheese futures market and cash market (Exchange) are interdependent. A more competitive and larger volume cash market might encourage broader participation in the futures market. Similarly, a larger volume, more viable futures market could affect prices in the cash market.

The lack of reliable and broadly available market information limits market participation. Currently, the entire dairy industry relies on the judgment of a small number of firms to signal prevailing supply and demand conditions. These signals, which are based on a tiny number of transactions, may or may not be reliable, and may be subject to manipulation. Government and the industry at large could take steps to improve the amount and reliability of market information available to farmers, cheese manufacturers and other market participants.

The cheese market is a national market. No state, acting by itself, can effectively resolve market problems that are national in scope. Nor can government resolve perceived problems in the cheese market without the effective support and cooperation of the market participants. At this time, there is no effective alternative to the Exchange as a price discovery mechanism for bulk cheese. All market participants, including the Exchange members themselves, are to some extent "captives" of current market arrangements. Real solutions will require national action, and broad industry support.

Although the Exchange is dominated by a handful of traders, this is not true for cheese manufacturing and marketing nationally. The largest four cheese manufacturers make about 30 percent of U.S. cheese. The largest four marketers account for about 38 percent of all cheese marketed. Thus, if a cheese pricing market can be developed that reflects the broader national organization, there is the potential for far more competitive and accurate price discovery.

RECOMMENDATIONS

At this time, DATCP and the authors of the report recommend the following steps:

- The dairy industry should seriously examine alternatives to the Exchange as price discovery mechanisms for cheese. The industry could adopt, among other things, changes to reflect the current structure and scope of the cheese industry. An electronic exchange could accommodate a wider range of trading activity and allow broader access and participation via a decentralized and direct exchange between buyers and sellers. Some preliminary steps in this direction have already been taken by the industry.
- To facilitate the development of more effective cash and futures markets, the federal government and the dairy industry should develop more timely, reliable and broadly-available information related to milk and cheese market conditions. Improving the existing U.S. Department of Agriculture market information is one way. USDA has been considering changes to improve bulk cheese price reporting for the spot market. USDA should also consider extending the information reported, so that it is representative of regional markets and includes timely production and inventory data for specific types of cheese.
- Congress should consider whether federal regulatory authorities should examine the National Cheese Exchange more closely, given its central role in the entire dairy pricing system.
- Federal antitrust authorities, in cooperation with the Wisconsin Department of Justice, should review this report to determine whether there may be any violations of antitrust law that warrant further investigation.
- USDA and the Commodity Futures Trading Commission should review this report to determine whether they should take action to regulate business practices related to the marketing of cheese, including activities on the National Cheese Exchange.
- The Wisconsin Department of Agriculture, Trade and Consumer Protection will propose rules, under the state's "Little FTC Act," to regulate anticompetitive "trading against interest" on the National Cheese Exchange. The department will propose preliminary draft rules to the DATCP Board in the near future. Rules, if adopted by DATCP, would be enforceable in court. Rule violations would be subject to substantial criminal penalties or civil forfeitures. Persons suffering monetary losses because of rule violations could also sue the violator for double damages.

Regulatory action, by itself, will not solve the underlying problems identified by this report. Real solutions must address the current lack of market information and the need for an effective price discovery mechanism that can serve as the basis for pricing bulk cheese. The problem is national in scope, and solutions will require broad government and industry support on a national level.

NATIONAL CHEESE EXCHANGE INVESTIGATION

QUESTIONS AND ANSWERS

March 19, 1996

1. What prompted this investigation?

The cheese industry and the dairy economy are very important to Wisconsin. There has long been concern about the buying and selling of cheese and, in particular, cheese transactions on the National Cheese Exchange. Trading on the National Cheese Exchange, located in Green Bay, Wisconsin, has a major influence on milk and cheese prices throughout the entire nation.

In 1990 and 1991, extreme volatility in cheese prices on the Exchange prompted inquiries and concern about Exchange activities. A preliminary study by University of Wisconsin economists suggested the need for a more in-depth study related to cheese buying and selling practices.

2. Who conducted the investigation?

The Wisconsin Department of Agriculture, Trade and Consumer Protection (DATCP) has authority to investigate business practices in Wisconsin. In February, 1992, DATCP and the University of Wisconsin-Madison College of Agricultural and Life Sciences entered into an agreement to conduct an investigation of cheese buying and selling practices, including transactions on the National Cheese Exchange.

The UW Food Systems Research Group conducted the investigation under contract with DATCP, pursuant to DATCP's statutory authority. The UW's Food Systems Research Group also authored the investigative report. The principal authors, Professors Willard F. Mueller and Bruce W. Marion, were assisted by research scientists Maqbool Sial, Ph.D., and Frederick Geithman, M.S. (See credentials attached.)

3. Who determined the scope of the investigation?

The UW researchers, in consultation with DATCP, determined the scope of the investigation. The researchers pursued those lines of inquiry which they felt were important. As experts on the organization and competitiveness of the U.S. food marketing industries, the researchers decided what information they needed for the investigation. DATCP used its subpoena power to obtain business information which the researchers needed.

4. What does this investigation mean for farmers and the general public?

Trading on the National Cheese Exchange is the main determinant of nationwide cheese prices. Cheese prices, in turn, have a direct impact on milk prices paid to farmers. Prices on the National Cheese Exchange also figure into the basic formula price under federal milk marketing orders.

In effect, the entire dairy industry relies on the judgment of a small number of firms to signal prevailing supply and demand conditions. These signals, which are based on a tiny number of transactions on the National Cheese Exchange, may or may not be reliable, and may be subject to manipulation by individual firms trading on the Exchange.

This report suggests that government and the dairy industry should take action to promote a fairer, more broadly based, and more competitive "price discovery mechanism" for cheese and milk. This will not, by itself, guarantee higher prices to farmers. But it will provide greater assurance that prices accurately reflect supply and demand, and are not being unfairly manipulated.

The dairy industry as a whole, and the various competing companies within that industry, have a stake in assuring that dairy pricing takes place in the context of broadly competitive markets that fairly reflect underlying market conditions. Although the National Cheese Exchange has a less direct link to consumer prices, the public at large also stands to benefit from broadly based competitive markets.

5. Did the investigation find any law violations?

The investigation did not find any evidence of an illegal conspiracy between companies to fix prices. However, the investigation does conclude that individual companies may "trade against interest" on the National Cheese Exchange in order to affect prices to their advantage on the larger cheese market. DATCP is proposing rules to prohibit anticompetitive "trading against interest" on the National Cheese Exchange. However, state regulation cannot fully address market problems that are national in scope. Congress and federal regulators should consider what federal regulation may be appropriate.

Regulatory action, by itself, will not solve the underlying problems identified by this report. Real solutions must address the current lack of market information and alternative "price discovery" mechanisms. The problem is national in scope, and solutions will require broad government and industry support on a national level.

6. Why is the National Cheese Exchange so important, if only a small amount of cheese is traded there?

During the period covered by this investigation, less than one half of one percent of all bulk cheese was sold on the National Cheese Exchange. But the exchange has a major nationwide impact on bulk cheese prices. About 90 to 95 percent of all bulk cheese is sold under long-term cheese supply contracts in which the price is tied directly to prices on the Exchange. Because cheese supply contracts throughout the nation are pegged directly to Exchange prices, the Exchange has a market impact that is far out of proportion to the amount of cheese traded there.

Because cheese is the most important manufactured dairy product, cheese prices have a direct impact on milk prices paid to farmers. Exchange prices largely determine nationwide cheese prices, and hence are directly linked to milk prices. Exchange prices are the major component in the "basic formula price" used in federal milk marketing orders.

Although the cheese industry as a whole is not unduly concentrated, trading on the National Cheese Exchange is dominated by a small number of firms. Because the Exchange has such a disproportionate impact on the overall cheese market, individual traders may have both the opportunity and the incentive to influence overall market prices to their advantage.

In effect, the entire dairy industry relies on the judgment of a small number of firms to signal prevailing supply and demand conditions. These signals, which are based on a tiny number of transactions on the National Cheese Exchange, may or may not be reliable, and may be subject to manipulation by individual firms trading on the Exchange. The report suggests that government and the dairy industry should take action to promote a fairer, more broadly based, and more competitive price discovery mechanism for cheese and milk.

7. If the National Cheese Exchange is an unreliable indicator of market conditions, why does the entire cheese industry use Exchange prices as the basis for pricing bulk cheese contracts?

At this time, there is no effective alternative to the National Cheese Exchange as a price discovery mechanism for bulk cheese. All market participants, including the Exchange members themselves, are to some extent "captives" of current market arrangements. The cheese industry needs an effective price discovery mechanism; but this report suggests a need to replace the National Cheese Exchange or enhance its competitive performance.

Among other things, this report suggests that government and industry should seek ways to enhance market information and encourage broader market participation. A more competitive and larger volume cash market might encourage broader participation in the fledgling "futures" markets for milk and cheese. More viable "futures" markets might in turn affect prices in the cash market.

Although the National Cheese Exchange is dominated by a handful of traders, this is not true of the underlying cheese manufacturing and marketing industry. The largest 4 cheese manufacturers account for only about 30 percent of U.S. cheese, and the largest 4 marketers account for only about 38 percent of all cheese marketed. If the current, highly concentrated, cheese pricing market could be replaced by a more inclusive market that reflects the more competitive organization of the industry itself, there is the potential for far more competitive and accurate price discovery.

8. Did the companies cooperate with the investigation?

Members of the National Cheese Exchange generally cooperated to a reasonable degree. Some companies were more cooperative than others. The report authors believe that they obtained the essential information needed to perform a thorough investigation.

9. How were "trade secrets" handled in the report?

The authors' analysis is based, in part, on proprietary information which DATCP subpoenaed from companies that trade on the National Cheese Exchange. The authors, DATCP and the Wisconsin Department of Justice worked to ensure that the report contains all of the information which the authors believe is necessary, without disclosing legitimate "trade secrets" that are protected by law.

The authors obtained substantial proprietary information from Kraft General Foods, Inc., the most important trader on the Exchange during the period covered by the report. The authors have temporarily deleted certain Kraft business data from the report, pending prompt court resolution of a good faith dispute with Kraft as to the trade secret status of those data. The temporary deletions, which are identified in the report, do not affect the report's analysis or conclusions. Kraft has agreed to a prompt court resolution of the trade secret issues, and the data will be made public if and when a court approves their release. The authors, DATCP and DOJ have taken this approach so that release of the investigative report would not be delayed pending litigation of Kraft's trade secret claims.

10. Does the report focus on Kraft to the exclusion of other companies?

The report examines the trading activity of 9 leading traders on the National Cheese Exchange, who together accounted for 94 percent of all sales and purchases during 1988-1993. A more detailed analysis of Kraft trading merely reflects its preeminence as a trader on the Exchange during the period covered by the investigation. Kraft accounted for 74 percent of all sales on the Exchange during the period 1988-1993.

Kraft also showed the most significant reversal in trading patterns on the Exchange. Prior to 1987, Kraft was primarily a buyer of cheese on the Exchange, just as it was primarily a buyer off the Exchange. But Kraft was almost exclusively a seller on the Exchange during the period 1987-1993, even though it was primarily a buyer off the Exchange.

This reversal occurred at the same time that trading activity on the Exchange became more important in determining cheese prices. During 1980-1987, cheese prices were strongly influenced by the government dairy price support program. As support prices declined, cheese prices became more market driven, and trading on the Exchange became more important in determining nationwide prices for bulk cheese.

11. Why has it taken so long to complete the investigation?

The researchers examined massive amounts of information supplied by the major traders on the National Cheese Exchange. The researchers also examined large amounts of information from public sources. The researchers thoroughly examined all of the issues which they considered important to understanding the organization of the bulk cheese market, and the conduct of cheese buyers and sellers.

In order to complete the investigation, it was necessary to subpoena and analyze voluminous company records related to cheese transactions and business operations. The process used to obtain information was lengthy, due in part to the proprietary nature of the information and the reluctance of some companies to cooperate in providing the information.

12. How was this investigation funded?

This investigation was primarily financed by special grants appropriated annually by the U.S. Congress for the University of Wisconsin-Madison. The UW supplemented the grant monies, to some extent, from other sources. No DATCP moneys were used to pay for the UW research. DATCP used existing legal and other staff to assist the investigation, as part of their normal duties.

About the Authors

Willard F. Mueller is Vilas Research Professor of Agricultural Economics, Professor of Economics, Professor in Law School, emeritus, at the University of Wisconsin-Madison since 1969. He has also taught at the University of California-Davis; University of Maryland; Michigan State University; and American University. From 1961-68, he was Director of the Bureau of Economics, Federal Trade Commission; and from 1968-69, he served as Executive Director of the President's Cabinet Committee on Price Stability. From 1973-1986, he was chairman of a 15-state research consortium to study the Organization and Performance of the U.S. Food System. He served the Industrial Organization Society as Vice-President (1988-89) and as President (1989-90). Mueller has received many honors and awards, including election as a Fellow of the American Agricultural Economics Association in 1976; awards for Professional Excellence in Recognition of: Quality of Research Discovery (1988); Quality of Communication (1985); Quality of Policy Contribution (1980), American Agricultural Economics Association. He is a member of the Advisory or Editorial Boards of *The Antitrust Bulletin*, 1979-present; *Journal of Reprints for Antitrust Law and Economics*, 1979-present; *Review of Industrial Organization*, 1984-present; *Antitrust Law & Economics Review*, 1986-present. He is author or co-author of a dozen books and monographs and numerous professional articles dealing with issues of competitive behavior and public policy in a market economy.

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News

NATIONAL CHEESE EXCHANGE
INVESTIGATION REPORT RELEASED

Release: 3/19/96
Contact: Prof. Bruce Marion
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Embargoed for 3:00 p.m. release at briefing

MADISON--A report on the Green Bay, Wisconsin National Cheese Exchange (NCE) as a mechanism for determining bulk cheese prices was released today by the Wisconsin Department of Agriculture, Trade and Consumer Protection and the University of Wisconsin-Madison College of Agricultural and Life Sciences.

In 1991, a large drop in cheese prices occurred on the National Cheese Exchange, which serves as the pricing mechanism for most bulk cheese transactions in the United States. This prompted concern among dairy farmers and others regarding the Exchange's activities. A preliminary investigation by economists at the University of Wisconsin-Madison suggested that an in-depth investigation take place.

In February 1992 the Wisconsin Department of Agriculture, Trade and Consumer Protection and the College of Agricultural and Life Sciences at UW-Madison agreed to carry out the in-depth investigation. CALS agricultural economists analyzed data from a number of companies that are major buyers and sellers of bulk

(more)

NATIONAL CHEESE EXCHANGE INVESTIGATION--add one cheese on the NCE. They analyzed NCE prices from 1988 through 1993, a period that saw a sharp increase in the volatility and range of cheese prices.

The report authors are Bruce W. Marion, professor, Department of Agricultural Economics; and Willard F. Mueller, emeritus professor, Departments of Agricultural Economics, Economics, and the Law School; assisted by Maqbool Sial, research scientist, Department of Agricultural Economics; and Frederick Geithman, research scientist, Department of Agricultural Economics.

The report is the culmination of a comprehensive three-and-one-half year investigation jointly conducted by the state agency and the Food System Research Groups of the Department of Agricultural Economics, UW-Madison.

In addition to affecting all companies that buy and sell cheese, NCE prices have a particularly strong effect on farmers who produce milk for cheese. The report lists implications of cheese selling on the NCE and makes corrective recommendations. Copies of the report are available from the Department of Agriculture, Trade and Consumer Protection.

The research conducted by the College was funded by the U.S. Department of Agriculture and the Wisconsin Department of Agriculture, Trade and Consumer Protection.

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Take #10

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PRESS RELEASE

March 20, 1996

GRONEMUS CALLS FOR ACTION AGAINST "BIG CHEESE"

"It's about time!", With these words, State Representative Barbara Gronemus, the Ranking Minority Member of the Assembly Committee on Agriculture, hailed the release of the exhaustive study of the National Cheese Exchange by the UW-College of Agriculture and Life Sciences.

The study, done for the Wisconsin Department of Agriculture, Trade and Consumer Protection, revealed the domination of the Cheese Exchange by large traders, especially, Kraft General Foods, Inc., and their ability to control cheese prices; prices, which in turn influence the price of milk paid to Wisconsin dairy farmers.

Gronemus said the study shows that traders influence the Cheese Exchange to their own benefit to the detriment of dairy farmers, who receive reduced prices for their milk.

"It's time for action", Gronemus said. "This study confirms what many of us in agriculture have long suspected - that big companies manipulate the Cheese Exchange for their own financial benefit". Gronemus noted that, while a 1988 investigation of the Cheese Exchange by the Attorney General discovered no

PRESS RELEASE

March 20, 1996

collusion, farmers have continued to be held captive by the operations of the Exchange. "Now that we have general evidence", Gronemus said, "the Department Of Agriculture and the Attorney General should move against the Exchange and its traders without delay to recover the farmer's share of their ill-gotten gains; I call upon the Attorney General and Secretary Tracy to move promptly". Further, Gronemus said, "Every cent that they recover should go right back to the dairy farmers!"

While Gronemus acknowledged that dairy co-ops may have claims, she stressed that farmers have been the persons who were primarily injured by the predatory practices of the "big cheese" companies. "Kraft and its brethren have long had their way at the Cheese Exchange. Now that the truth is out, it is time that Wisconsin's hard-working dairy farmers get their measure of justice", Gronemus concluded.

Trade & Consumer Protection

Wisconsin Department of Agriculture, Trade and Consumer Protection

April 1996

Green Bay is prosecuting landlords breaking the law

The City of Green Bay, Brown County District Attorney and the Department have made it a priority to prosecute repeat-offender landlords. And the first criminal complaint has been filed.

Concern about run down neighborhoods in Green Bay and danger to tenants is leading to a crackdown. Repeat-offender landlords may go to jail.

Green Bay Mayor Paul Jadin, Brown County District Attorney John Zakowski, and Wisconsin Bureau of Consumer Protection Regional Manager Judy Cardin have announced the formation of a tri-agency agreement, giving priority to prosecution of repeat-offender landlords.

"Most landlords are honest business people providing decent places to live," says Cardin. "But we do have rental units in Green Bay that are seriously deteriorating. Rent-paying families are entitled to a safe place to live."

The Green Bay Building Inspection Department will refer repeat-offenders to the Bureau of Consumer Protection for investigation. The Bureau

enforces the Residential Rental Practices Law. Brown County District Attorney Zakowski will prosecute cases brought to him by the Bureau.

A similar agreement in Milwaukee led to the prosecution of 13 landlords since 1992. Ten of those landlords went to jail.

Consumers can also protect themselves by knowing the law, says Cardin of the Bureau of Consumer Protection:

- Landlords must tell prospective tenants about all uncorrected building code violations.
- Landlords cannot rent condemned property.
- Landlords must put repair promises in writing before any money changes hands.
- Question whether serious defects will be repaired. It is probably best to seek housing elsewhere.
- Consumers can check with the Bureau of Consumer Protection to see if complaints have been filed against a landlord: (800) 422-5110. ■

CRIMINAL COMPLAINT STATE OF WISCONSIN

vs

Gerald R. Alsteen
1169 Law Street
Green Bay, WI 54301

A Green Bay landlord has been charged with numerous violations involving low-income tenants and prospective tenants, including taking earnest money and not delivering the agreed upon apartment.

For example, Rebecca E. Wanty says she gave Landlord Gerald R. Alsteen \$700 to hold an apartment for her and filled out a lease agreement. But when she went to pick up the keys for the place, Alsteen didn't show up and the current tenants hadn't moved out. Later Alsteen called up Wanty and asked for an additional \$300.

When Wanty said she wanted her money back because the terms of the lease had not been kept, Alsteen allegedly said that she would have a hard time getting the money out of him because he had spent it on other things.

All told, Alsteen allegedly failed to return all or part of the earnest money paid to him by three women. Alsteen also failed to put promised repairs in writing, which is also a violation of the law.

The criminal complaint charges Alsteen with 10 counts of violating Wisconsin's landlord-tenant law. If convicted Alsteen could be fined up to \$5000 and imprisoned up to one year for each of the 10 counts. ■

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NEWS

Trade & Consumer Protection

**Wisconsin
Department of Agriculture
Trade & Consumer Protection**

This publication is dedicated to men and women who protect the people of Wisconsin.

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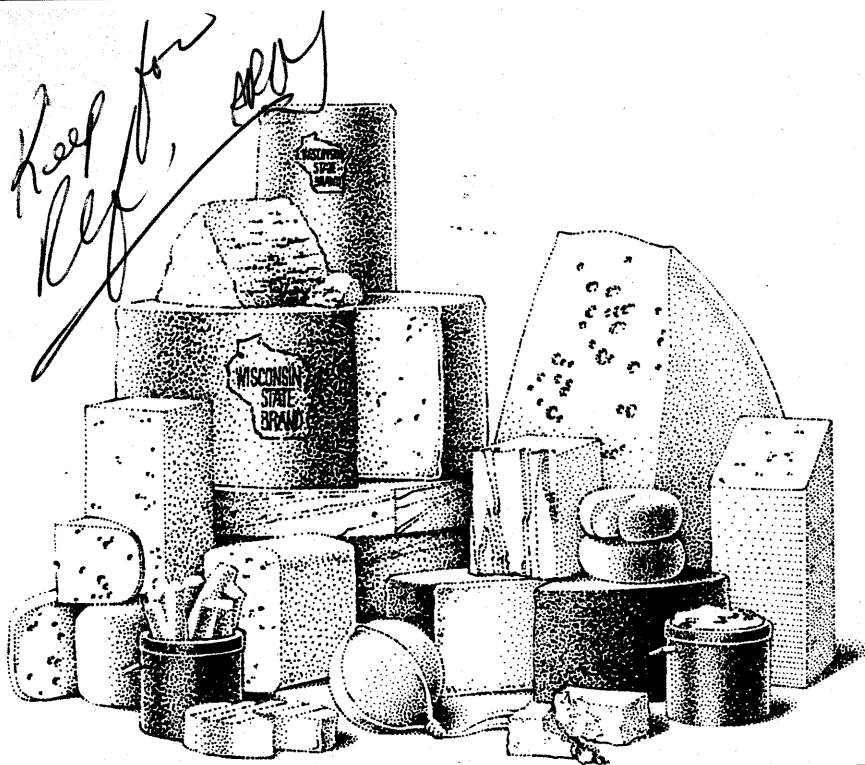
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Milk and cheese prices manipulated?

“The Cheese Exchange may facilitate price manipulation by individual firms. But the report found no evidence of a conspiracy between cheese companies to fix prices.”

Reprinted from Legal E's

The National Cheese Exchange is a little known cash auction market for bulk cheese, located in Green Bay, Wisconsin. Members of the Exchange meet every Friday, for about 1/2 hour, to buy and sell bulk cheddar cheese in carload quantities. Trades are hand-recorded on a board. But trading on this little known Exchange is dominated by some of the nation's largest food companies, and prices on the Exchange play a key role in determining milk and cheese prices for the entire nation!

On March 19, 1996, the Department and the University of Wisconsin released a major investigative report on the Exchange. The report culminates a 3 1/2 year investigation. UW economists authored the report after sifting through mountains of evidence subpoenaed by the Department. The report raises serious concerns about the Exchange, including concerns about possible price manipulation

affecting nationwide milk and cheese prices. According to the report:

- The Exchange has a market impact that is far out of proportion to the amount of cheese traded there. During the period covered by the report, less than 1/2 of one percent of the nation's bulk cheese was sold on the Exchange. But 90 to 95 percent of the nation's bulk cheese (not just cheddar) is sold under contracts whose prices are pegged to prices on the Exchange. Because cheese is the most important manufactured dairy product (commanding 85 percent of Wisconsin milk and 33 percent of U.S. milk), Exchange prices also have a powerful impact on milk prices paid to farmers. Exchange prices are a major component of the “basic formula price” used in federal milk marketing orders.
- Although the cheese industry is not highly concentrated, trading on the Exchange is dominated by a handful of companies. During the

period 1988-1993, four companies accounted for 88 percent of all cheese sales on the Exchange. Kraft General Foods, Inc., owned by Philip Morris Companies, Inc., accounted for 74 percent of all sales. The four largest buyers accounted for 81 percent of all cheese purchases on the Exchange. Beatrice Cheese, Inc., owned by Con Agra, Inc., was the leading buyer with 35 percent of all purchases on the Exchange.

- When government price supports dropped after 1987, the range and volatility of milk and cheese prices increased sharply. Trading on the Exchange became even more important in determining milk and cheese prices throughout the nation. Milk and cheese prices are broadly determined by national supply and demand. But after 1987, traders on the Exchange had a greater opportunity and incentive to influence cheese prices to their advantage.

- After 1987, key traders on the Exchange reversed their pre-1987 trading patterns. Several leading buyers off the Exchange became mainly sellers on the Exchange, and vice versa. Kraft, the nation's largest cheese company, became almost exclusively a seller on the Exchange, although it is mainly a buyer off the Exchange. In some cases, it appears that Kraft may have sold on the Exchange at lower prices than it could have received off the Exchange.

- This raises the question whether companies may "trade against interest" on the Exchange in order

to affect prices to their advantage in the overall milk and cheese market. For example, if a buyer of bulk cheese can reduce the Exchange price (and hence prices in the overall market) by selling a small amount of cheese on the Exchange at a low price, that buyer may be able to reduce its nationwide procurement costs. Statistical analysis suggests that leading Exchange sellers, especially Kraft, had a significant negative impact on Exchange prices.

- According to the report, each one cent decline in Exchange prices lowered Kraft's procurement costs by more than \$10 million annually. But because of its brand name recognition, Kraft was able to keep its retail prices relatively constant. This boosted Kraft's profits, at least in the short run. By contrast, farmers tend to suffer when bulk cheese prices drop.

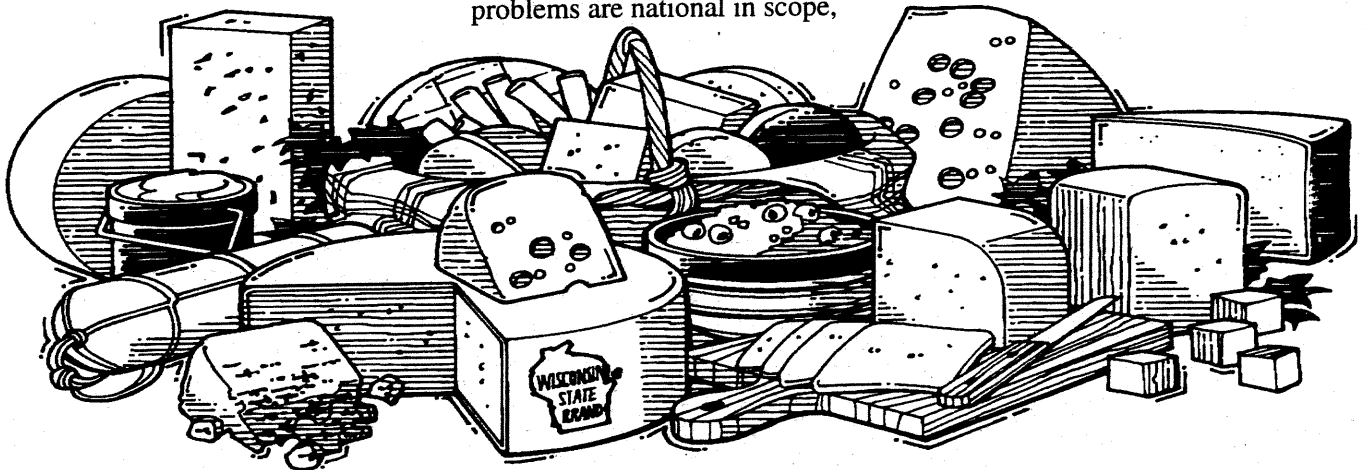
- The authors conclude that the Exchange was not a reliable indicator of underlying market conditions during 1988-1993. They also conclude that, as currently organized, the Exchange may facilitate price manipulation by individual firms. But the report found no evidence of a conspiracy between cheese companies to fix prices.

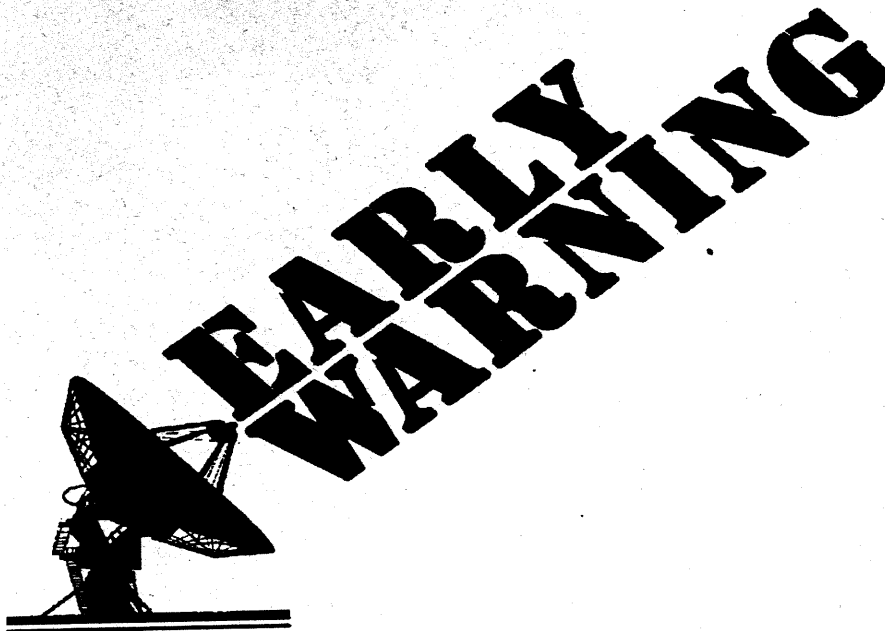
The department is proposing rules to prohibit anticompetitive "trading against interest" on the National Cheese Exchange. But state regulatory action, by itself, will not solve the underlying problems identified in this report. The problems are national in scope,

and solutions will require more effective and broadly based "price discovery" mechanisms for cheese. Eventually, the dairy industry may develop the kind of broad-based cash and "futures" markets which exist for many other commodities. But at the moment, there is no effective alternative to the National Cheese Exchange. Prompted by this report, Governor Thompson has announced the formation of a state task force to suggest ways to improve the National Cheese Exchange. The task force will probably look at a variety of options, including the department's proposed rules. The DATCP Board has deferred action on the rules pending consideration by the task force.

Several federal agencies are also looking at the issue, and Congress is planning to hold hearings. Solutions will require effective government and industry support at the national level. Wisconsin, which produces 30 percent of the nation's cheese, has a big stake in the outcome. ■

UW Professors Willard Mueller and Bruce Marion were the principal authors of the Cheese Exchange report. They were assisted by research scientists Maqbool Sial, Ph.D. and Frederick Geithman, M.S. (Maqbool now works in DATCP's Bureau of Trade Practices.) Several DATCP staff members worked on the investigation. For further information about the report, contact Carol Trypus in the Bureau of Trade Practices.





Our early warning to state charities and investors

To keep people in Wisconsin from buying into a coupon book deal that sounded too good to be true, the Bureau of Consumer Protection issued an early warning.

Wisconsin investors and charities got an early warning this month from the Bureau of Consumer Protection about a company marketing fund-raising coupon books.

The early warning press release was carried by the Milwaukee Journal-Sentinel and the Associated Press as well as Milwaukee, Green Bay and Madison TV stations.

Some investors have paid up to \$150,000 to the California company involved to market the coupons for breakfast cereal and coffee. And nonprofit groups all over the state—like the Green Bay East High School Band—have sold the coupons to raise funds.

After our early warning, California law enforcement officials filed a lawsuit against United Grocers Clearinghouse (UGC) for two million dollars in restitution for customers and distributors and at least two million dollars in civil penalties for violations of California law.

The lawsuit alleges that UGC is operating a Ponzi scheme. "Defendants receive money from investors," says the California lawsuit, "and make payments in products paid for from money obtained from later investors rather than from profits of the underlying business venture, thereby cultivating an illusion that a legitimate profit-making business opportunity exists and inducing further investment. When this house of cards falls apart, both consumers and distributors suffer losses."

Cereal and coffee manufacturers are not involved in the promotion and are concerned about implications that they are, according to Judy Cardin of the Bureau of Consumer Protection in Green Bay.

The \$30 coupon books contain 30 coupons. Consumers make a selection of cereal, for example, mail in one coupon, and receive one box via UPS. Consumers

Can stay out of jail with restitution

Craig Gavaert has been found guilty in Outagamie Circuit Court of seven criminal counts of violating the home improvement trade practices code. Consumer Protection Bureau Investigator Doug Augustine coordinated the investigation.

Consumers alleged that Gavaert took their money for reroofing jobs, tore off existing roofs, and then didn't come back. Water damage took place because the homes were exposed to rain.

In an attempt by the Outagamie County District Attorney's Office to get money back to the victims, Gavaert will have Huber privileges his first year in jail to enable him to make \$200 a month restitution payments. The other three years of jail were stayed if he continues the \$200 payments.

Total restitution to seven victims is \$25,216. ■

repeat the process to get the next box.

The Bureau of Consumer Protection has sent a warning letter to a Wisconsin distributor for:

- Telling customers they will receive products within 7-10 days, when in fact it is currently taking 3-4 weeks.
- Misrepresenting to customers how long United Grocers Clearinghouse has been in business.
- Misrepresenting that a nonprofit group or cereal manufacturers were participants in the promotion.
- Using the names of nonprofit organizations as endorsers or participants in fund raisers without a signed agreement that includes a disclosure to the nonprofit organization that they can be held jointly accountable for law violations.
- Selling coupon books without a required written three-day right to cancel or disclosure of redemption conditions. ■



State of Wisconsin
Tommy G. Thompson, Governor

Department of Agriculture, Trade and Consumer Protection

Alan T. Tracy, Secretary

2811 Agriculture Drive
Madison, Wisconsin 53704-6777

PO Box 8911
Madison, WI 53708-8911

*File
Apt*

May 14, 1996

Roger E. Wyse, Dean
College of Agricultural and Life Sciences
University of Wisconsin-Madison
140 Agriculture Hall
1450 Linden Drive
Madison, WI 53706

Ayse Somersan, Dean
Cooperative Extension
University of Wisconsin-Extension
601 Extension Building
432 North Lake Street
Madison, WI 53706

Dear Deans Wyse and Somersan:

I am writing to express my appreciation for the contributions that faculty and staff from the College of Agricultural and Life Sciences and Cooperative Extension have been making to improve the dairy economy of Wisconsin. Their efforts have been outstanding. I would like to single out three UW projects with which our department has been associated.

Professors Fritz Mueller's and Bruce Marion's comprehensive study of bulk cheese pricing and the National Cheese Exchange has provided invaluable information and insight into the mechanisms for pricing bulk cheese. The study raises serious concerns about the Exchange as a cheese pricing mechanism. Because of their work, I am hopeful that further action at both the state and federal levels will result in improvements to the bulk cheese market.

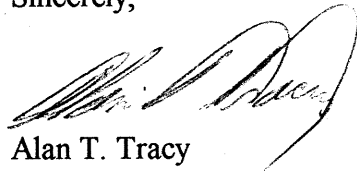
Professors Tom Cox, Ed Jesse and Bob Cropp of the Department of Agricultural Economics have made important contributions to recent efforts to reform federal dairy policy. Their expertise in and economic modeling of dairy policy and markets provided Representative Steve Gunderson and the Upper Midwest Dairy Reform Coalition with reliable and accurate information to argue for federal dairy reform. We recognize that the fight is not yet over and that consolidation of the federal milk marketing order system over the next few years will require the Coalition to continue to work together, with UW dairy economists, to achieve a federal dairy program that is equitable to Wisconsin producers.

I would also like to express appreciation for the Center for Dairy Profitability. The Center's director, Professor Bruce Jones and CDP staff are working with the state's Dairy 2020 Initiative to provide the kinds of services and programs our dairy industry needs. For example, Dairy 2020 identified the need for training in management skills for our new and expanding dairy farm operators. The Center's Agribusiness Executive Management training program will help our dairy producers to be successful and competitive. I especially appreciate your personal efforts to provide the CDP with increased resources to make a good program stronger in the face of overall tight budgets.

Dean Wyse
Dean Somersan
May 14, 1996
Page 2

In the tradition of "The Wisconsin Idea," University faculty and staff have been working in partnership with the state's dairy industry, our department, and other state and federal entities to analyze and solve problems and meet the challenges we face as we move into the 21st century. Our department looks forward to continuing our strong relationship with UW to address the concerns of our agricultural community and Wisconsin's consumers.

Sincerely,



Alan T. Tracy
Secretary

cc: Governor Thompson
State Representative Ott
State Senator Lasee

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608 266 3970

P.2



TOMMY G. THOMPSON

Governor
State of Wisconsin

File

For Immediate Release — May 14, 1996
Contact: Rod Hise (608) 266-9806

GOVERNOR APPOINTS CHEESE PRICING TASK FORCE

MADISON — Gov. Tommy G. Thompson today announced the appointment of the Task Force on Cheese Pricing.

“Wisconsin is fortunate to be home to the National Cheese Exchange,” Gov. Thompson said. “The Task Force I appointed today will facilitate a discussion among the stakeholders of the cheese pricing system and make recommendations to improve the current system for the benefit of the dairy industry and consumers.”

The Task Force will be chaired by Fred Kasten, President and CEO of Robert W. Baird & Co. of Milwaukee. The other Task Force members appointed today by the governor are:

- Gary Anderson, dairy farmer, Cecil
- Bob Burns, President, Beatrice Cheese, Waukesha
- Marsha Glenn, Vice President, Kraft Foods, Glenview, IL
- Bernard Golbach, President, Master's Gallery Foods, Plymouth
- Richard Gould, President, National Cheese Exchange, Green Bay
- Will Hughes, Wisconsin Federation of Cooperatives, Madison
- Ed Jesse, Associate Dean, UW-Madison College of Agriculture and Life Sciences, Madison
- Larry Lemmenes, President and General Manager, Alto Dairy Cooperative, Waupun
- Secretary William McCoshen, Department of Development, Madison
- O'Neill McDonald, Regional President, Supervalu Stores, Milwaukee
- Jon Peterson, dairy farmer, Cashton
- Jack Strum, President, A. Sturm and Sons, Manawa
- Bob Thelen, dairy farmer, La Farge
- Secretary Alan Tracy, Department of Agriculture Trade and Consumer Protection, Madison
- Wilfrid Turba, DATCP board member, Elkhart Lake
- Deborah Van Dyk, Schrieber Foods, Green Bay
- Bob Wegner, President, Weyauwega Milk Products, Weyauwega

The Task Force will complete its work and issue a report to the governor by January 1, 1997.

Wisconsin is the world's number one cheese maker, producing one-third of the world's cheese. Cheese prices directly affect the price received by Wisconsin's 27,000 dairy farmers for their milk.

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Attorneys at Law in
Milwaukee and Madison, Wisconsin
West Palm Beach and Naples, Florida
Phoenix, Arizona

Quarles & Brady

May 21, 1996

File, Al

Rep. Alvin Ott
State Capitol, Room 318-N
P.O. Box 8953
Madison, WI 53708

RE: Washington Hearing on National Cheese Exchange

Dear Al:

As you may know, hearings were held in Washington on May 15 and 16 on the National Cheese Exchange ("NCE"). The hearings were held by the Subcommittees on Risk Management and Specialty Crops and on Livestock, Dairy and Poultry of the House Committee on Agriculture.

Appearing at the hearing were Betsy Holden, Executive Vice President of Kraft Foods and General Manager of the Kraft Cheese Division, DATCP Secretary Alan Tracy, and Professors Willard Mueller and Bruce Marion (authors of the report on the NCE which was released in March). These hearings provided the first critical review of that report. As the enclosed story from the *Milwaukee Journal Sentinel* indicates, both the methodology used and the conclusions reached in the report drew heavy criticism.

Kraft believes that the report is wrong because it is based on flawed analysis and repeated misuse of information. Kraft's actions on the NCE have always been honest, open and consistent with sound business principles. Kraft's trading has had no adverse effect on NCE prices.

Enclosed for your review (in addition to the *Journal Sentinel* article referenced above) are Betsy Holden's oral and written testimony as delivered at the hearings as well as the written testimony of James Lauderdale of Mid-American Dairymen, Inc., and Richard Gould, president of the NCE.

Kraft is proud of the role it plays in Wisconsin's dairy industry and the important contributions it makes to our state's economy. Please let me know if you would like more information about this issue.

Very truly yours,

QUARLES & BRADY

Peter C. Christianson
Peter C. Christianson

PCC:lmb
Enclosures

**ORAL TESTIMONY OF BETSY D. HOLDEN
EXECUTIVE VICE PRESIDENT, KRAFT FOODS
BEFORE THE SUBCOMMITTEES ON
RISK MANAGEMENT AND SPECIALTY CROPS
AND
LIVESTOCK, DAIRY AND POULTRY
OF THE HOUSE COMMITTEE ON AGRICULTURE
MAY 15, 1996**

Good morning, Chairman Ewing, Chairman Gunderson and other members of the Subcommittees. My name is Betsy Holden. I am an Executive Vice President of Kraft Foods and General Manager of the Kraft Cheese Division. As such, I am the senior executive with responsibility for Kraft's cheese business, a position I've held for about a year.

With me today, on my right/left, is Mr. Wayne Hangartner. Wayne is a Wisconsin native who began his career with Kraft in Green Bay some 44 years ago. Although he is now retired, Mr. Hangartner was the sole person with authority for Kraft's trading on the National Cheese Exchange during the period the professors reviewed.

I want to thank the Subcommittees for inviting us to testify. We appreciate the opportunity to set the record straight.

Mr. Chairmen, we believe the report is wrong. Wrong because it is based on flawed analysis and repeated misuse of information. We are confident that the facts, when looked at objectively, will tell the real story and, above all, will show three things:

- that the National Cheese Exchange works -- it accurately reflects supply and demand,
- that Kraft's actions were honest, open and consistent with sound business principles
- and that our trading had no adverse effect on Exchange prices.

Let me start first with the Exchange.

In assessing the reliability of this or any Exchange, perhaps the best common-sense test is to look at the confidence level of those who use it. With the National Cheese Exchange, you could not find a greater display of confidence. Year after year, nearly all cheese sellers, including farmer cooperatives, willingly use the NCE to price their cheese. There's no law or regulation requiring them to do so. They do it because they are confident the Exchange accurately reflects supply and demand.

They believe it because all dairy interests are represented on the Exchange and because the trading process itself provides strong protection against any member who might try to unduly influence the price of cheese. I think it's worth noting that despite the very investigation we are here to discuss, actual trading levels have tripled in the years since the investigation was announced. Whatever doubts others may have, members of the Exchange have clearly demonstrated a growing confidence in the NCE.

The second point I want to make is about Kraft's trading. Underlying all our actions is one simple goal: as a branded cheese company, we never want to run short of cheese. Running short carries the significant cost of lost sales, market share and shelf space.

We therefore manage our inventories to meet our projected needs, plus provide a safety supply to cover contingencies. At times, this practice has resulted in excess inventories which we then need to sell.

Whenever Kraft has had excess cheese to sell, it always sought to sell it when and where it believed it would receive the highest price, be that on or off the National Cheese Exchange. The record shows that, and nothing in the professors' report demonstrates otherwise.

Whatever allegations the report makes are based on nothing more than speculation and fabrication. With four years of study and 24,000 pages of Kraft documents, the report cannot produce a single instance where Kraft traded improperly. Why? Because none occurred.

The third point I want to make is that Kraft's trading had no adverse impact on Exchange prices.

Please keep in mind that 70% of Kraft's sales on the Exchange during the period in question were in response to bids initiated by other traders. Kraft was selling cheese for what other traders said it was worth. And no legal or regulatory body of any sort has ever found that meeting another trader's bid price constitutes manipulation.

In fact, the professors themselves repeatedly state in their report that there is no evidence whatsoever of collusion.

Even more fundamental, any suggestion that Kraft, with about a 15% share of the U.S. cheese business, has unilateral power over the marketplace and is able to move prices at will is simply ludicrous.

To the contrary, econometric analysis using the most sound and accepted techniques shows that Kraft's trading had minimal effect. In weeks when Kraft sold, the NCE price actually increased slightly, an average of about two-tenths of a cent. In weeks when others sold and Kraft did not, the price declined about 1.7 cents.

Kraft clearly does not have "market power" over the Exchange and its trading did not unduly influence prices.

What about the future? While we feel the Exchange functions well, Kraft has long been open to ideas for improvement. We have actively supported the advent of electronic trading. We would be open to proposals to add another day of trading, or perhaps to expand the styles of cheese traded.

Outside of the Exchange, Kraft strongly supported the development of cheese futures contracts.

We continue to be open to any other ideas that improve trading or price discovery.

As I close these remarks, I want to once again point out that Mr. Hangartner is no longer a Kraft employee. He is here on a voluntary basis to uphold the propriety of his actions and state categorically that he never traded against interest, nor did he ever receive instructions to do so. He is here to defend his own honor and the company he served for more than 40 years.

Mr. Chairmen, Mr. Hangartner and I thank you for this opportunity to set the record straight, and we would now be happy to answer your questions.

The *REAL* Facts

The National Cheese Exchange Works

- NCE Prices Reflect Supply and Demand
- Industry Confidence Is Proven By
 - The Tripling of Trading Since 1992
 - Industry Reliance on NCE for Transactions
- All Industry Interests Are Represented on the NCE

Kraft's Trading Made Good Business Sense

- Kraft Never Traded Against Its Self Interest
- ALL Kraft Sales Were At The Best Price Offered
- The Professors Could Not Identify A Single "Trade Against Interest"

Kraft's Trading Had No Adverse Effect On NCE Prices

- 70% of Kraft's NCE Trades Responded To Bids By Others
- The Professors Admit: "No Evidence of Collusion"
- Kraft Has No "Market Power" Over Milk or Cheese Supply
- The Professors' Econometrics – Properly Done – Prove Kraft's Trading Did Not Adversely Affect NCE Prices

Kraft Has Been And Remains Open To Change

2

**JOINT HEARING ON CHEESE PRICING
AND THE NATIONAL CHEESE EXCHANGE**

**WRITTEN TESTIMONY OF
BETSY HOLDEN, EXECUTIVE VICE-PRESIDENT
OF KRAFT FOODS, INC. AND GENERAL MANAGER
OF THE KRAFT CHEESE DIVISION**

**BEFORE THE SUBCOMMITTEES ON
RISK MANAGEMENT AND SPECIALTY CROPS AND
LIVESTOCK, DAIRY AND POULTRY
OF THE HOUSE COMMITTEE ON AGRICULTURE**

MAY 15, 1996

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I. INTRODUCTION

Good morning, Chairman Ewing, Chairman Gunderson, and other members of the Subcommittees. I am Betsy Holden, the Executive Vice President of the Kraft Cheese Division of Kraft Foods, Inc. I am the senior executive with responsibility for Kraft's cheese business and have been in this position about a year. I want to thank the Subcommittees for inviting me to testify. Accompanying me is Wayne Hangartner. Although Wayne is now retired, Wayne was the Director of Cheese Procurement and Inventories from 1988 until 1994. Wayne was the person responsible for Kraft's day-by-day cheese procurement and inventory control efforts and handled the week-by-week trading on the Exchange during the time period the Professors reviewed.

Kraft has been asked to address two issues at this hearing. *First*, how to eliminate price manipulation and trading against interest on the National Cheese Exchange? This first question presumes that such conduct has or could occur. Certainly, Kraft did *not* manipulate prices on the Exchange or ever trade against interest. Kraft also does not believe anyone is capable of manipulating the NCE. *Second*, Kraft has been asked whether there are ways to improve trading on the Exchange or whether there are better alternatives to the Exchange? Kraft has always been open to changes and alternatives, which I will touch upon after first responding to the Professors' Report.

Kraft's testimony is organized as follows. *First*, I provide some basic factual background on the dairy industry and the National Cheese Exchange ("NCE"). *Second*, I discuss some of the many problems with the analysis provided in the Report prepared by Professors Bruce Marion and Willard Mueller of the University of Wisconsin.¹ Finally, I discuss Kraft's response to the topics discussed in the invitation.

1. Willard F. Mueller, et al., *Cheese Pricing: A Study of the National Cheese Exchange*, A Report of the Food System Research Group, Department of Agricultural Economics, University of Wisconsin-Madison, Prepared For The Wisconsin Department of Agriculture, Trade, and Consumer Protection Investigation Into Cheese Pricing (March 1996) ("Report").