

Warming up for C.O.O.L.: American Viewpoint

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■ Introduction

Country of Origin Labeling (best known as COOL) has been a household name in the food sector for roughly two years, even though its origins go back much further than that. The reason that it is now getting so much attention is that in the 11th hour of debate over provisions to be included in the 2002 US Farm Bill, COOL was put on the table and basically became law. It was actually a congressional compromise over, what at that point in time was the hot topic, packer ownership of livestock.

We will probably never know for sure whether the passage of COOL was orchestrated by some crafty politicians or just perceived as being a benign issue. But no matter the reason for its passage, it has certainly become a politically charged and highly contentious issue in the US, Canada and elsewhere.

Sparks Companies, Inc. has been actively involved in the debate over the costs and potential economic benefits of COOL. I think it is important for everyone to be aware that we launched our COOL Consortium in late 2002 in conjunction with Steve Kay at Cattle Buyers Weekly. We have a consortium membership of Canadian industry and government stakeholders who have been supporting research and analysis on COOL. Some of my remarks today will draw on work that has been conducted for the Consortium.

Sparks Companies Inc very much appreciates the foresight that Canadian stakeholders had in making sure that objective information and analysis was put into the public record on this very important issue. Heaven knows that there has certainly been a lot of misinformation and shoddy analysis put forward and I can only assume that in the end, the facts and solid analysis will ultimately make a difference in how COOL is actually implemented.

■ Where are we at?

Where are we at this moment? What is the “American Viewpoint” on COOL? Unfortunately, this paper is being drafted in mid October 2003 to meet the publishing deadline for the conference proceedings. As of mid October, we do know the following:

- COOL is law and while currently voluntary, it is scheduled to become mandatory as of October 1, 2004
- USDA published (in the fall of 2002) preliminary guidelines for the voluntary COOL program that were highly prescriptive but legitimate given the requirements that were actually written into the law
- USDA published an estimate of the “record keeping costs” for COOL implementation and the price tag put on this was nearly \$2 billion US
- A comment period occurred in fall 2002 and winter 2003 to provide interested parties the opportunity to submit their opinions on COOL prior to the development and issuance of final implementation rules
- Industry hearings were held around the country to get input from industry stakeholders in the spring/summer of 2003
- A provision was included in the fiscal 2004 Agriculture Appropriations Bill that would delay funding of COOL for beef and pork until October 1, 2005
- An amendment was offered in the House by MN Congressman Collin Peterson, which would dramatically reduce the perceived cost burdens of COOL. This amendment has been tabbed COOL Lite
- USDA has taken all the public hearing submissions, submitted public comments, and has drafted final COOL implementation rules
- These rules (as of mid October 2003) are going through final inter agency approval within the US government and are scheduled for release sometime in the fall of 2003
- The 2004 Agricultural Appropriations bill looks like it will go to conference as part of a mini-omnibus bill and expectations are that the funding restriction for implementation of COOL on beef and pork will remain in place, effectively delaying a move to COOL implementation
- Once the final rule making process clears through government channels, the rules will be issued along with a complete benefit/cost assessment on COOL
- Indications are that the benefit/cost assessment will put a huge cost estimate on COOL and that few benefits will be identified

In final analysis, as of mid October 2003, COOL is travelling a rocky road. There remains today almost as much uncertainty about whether COOL will survive, as currently defined, as there was shortly after the Farm Bill was

passed. By the time that this conference is held, more should be known and an update of the situation will be provided in the presentation. Until then, the final outcome is highly speculative in nature and almost anything could happen. The odds favour delay of implementation and possibly a complete revamping or rescinding of the legislation. Bad legislation should not be implemented and, in my personal view, this legislation falls within that category with a capital B.

I was asked to provide an American viewpoint on COOL however, so I'll try and reflect the varying opinions and positions that have surfaced since the 2002 Farm Bill became law. It probably will not be too difficult to identify where Sparks stands on this issue or me personally, but in all fairness, there are some minor, positive features to the whole process of origin labelling. Unfortunately, most of these could be accomplished with a voluntary program driven by market incentives. There are few benefits to a mandatory program with high cost burdens on the commercial sector.

■ Arguments in Support of COOL

In the US, there are basically two primary camps when it comes to COOL and each one lies at the extreme ends of the spectrum. On one hand, the proponents of COOL argue very strongly that the “consumer” wants to know the origin of their food and this “right to know” should be part of normal business in the food industry. They carry this argument one step further by saying that because consumers have this desire to know where their food originates, they will be willing to pay a premium price for products that are of US origin because everyone knows that made in the USA is “better” or “best”, right? They argue that if consumers knew a product was of US origin, they would have preference for that product and that would improve the demand for US beef or US pork, etc., etc. And once again, everyone knows that if the demand for an end product by the consumer is stronger, that automatically means that the price for cattle or hogs will also be stronger. How many times have we heard that argument?

The major fallacy with this whole opinion or argument is that it is **not supported by ANY credible research** that we have been able to find. Most retailers will tell you that country of origin is way down the list of consumers concerns as it relates to issues in the meat case. In fact, the number of complaints or calls that major retailers have received from consumers asking for COOL is extremely small or non-existent. If the consumer just doesn't care about the origin of the product but merely wants to know that it is safe and wholesome, then why saddle the beef and pork supply chains with burdensome and costly regulations? The logic put forward by COOL proponents seems to be totally flawed, for if anything, the added cost burden to the various supply chains would probably reduce producer's margins rather than lead to enhanced

profitability. In effect, COOL would hurt the very constituents that it is purported to benefit.

Another weakness of the pro-COOL argument is the one that suggests that consumers have the right to know. Let's face it, if this was truly of importance to the proponents of COOL, then why not include labelling on food consumed in food service establishments and why exempt processed products such as hams, bacon and the like from being origin labelled. Consumers provide patronage to both retail food providers and food service providers and if the right to know argument holds any water, there should be no exceptions for food service establishments, and that is clearly not the case in the current COOL law.

So, why did COOL gain so much traction and actually get passed into law. The simple answer, in my opinion, is that it was pushed by several "populist politicians" that really don't understand the economics and dynamics of the meat industry. For those legislators that do have this understanding, the whole legislative effort seemed so preposterous that there was little belief that it would survive. Hence, little effort was put into stopping COOL before it could get passed. The whole COOL issue was never properly discussed and debated in Congress and got slipped in at the very end of the Farm Bill debate as a compromise to those that fought hard to get the packer ownership of livestock ban thrown out. It may very well be that the potential cost and damage from COOL could be more than what the costs and disruptions would have been from the packer ban. I'm not sure we'll ever really know but our analysis indicates that both situations will be disastrous for the US livestock and meat industry.

IF the proponents of COOL have an empty argument about the consumer benefits from origin labelling and **IF** these very proponents know that, then there is only one conclusion I can make in terms of why this bill was pushed so hard and it relates to trade and particularly trade amongst the NAFTA partners. It seems clear to me that the backers of COOL are the same industry stakeholders that tend to be anti trade and the politicians that supported COOL fall into that same camp. My fear is that support for COOL will be enhanced by the events of this summer surrounding the Canadian BSE situation as closure of the border has certainly resulted in or at least, been a major contributing factor to all time record high cattle prices (\$95-100/cwt. as this is being written) in the US. You can only imagine the smiles that have come on the faces of those pushing COOL as this is the type of short term price and profit lift US producers can/should expect if COOL could effectively close the border to Canadian live animal and product trade (both beef and pork). This is a chicken and egg argument but one we'll probably see floated from time to time.

■ The Cost Realities of COOL

Enough said for the PRO COOL argument. For those in the food industry in general and the meat industry in particular, there can be no question that COOL, as it currently stands, will be a highly costly and an extremely difficult program to implement and manage. A quick assessment of the supply chain changes that would be needed to effectively implement COOL, and still provide the consumer with full product choice, suggests that the costs would be totally prohibitive and that the only way for supply chain participants to survive would be to totally change how they are running their businesses. In fact, the “easy” way out would be to discontinue selling fresh Canadian beef or pork or selling products from Canadian cattle and hogs that are not imported as case ready products with proper origin identification already in place.

When digging into the guts of what would be required to meet the detailed requirements of COOL, two things jump out. One, an individual animal identification system would need to be developed in the US. Alternatively, a bullet proof segregation system on live cattle and hogs would need to be put into place which would cover the production and feeding stages of the supply chain. That system would need to be extended so that segregation could be continued at the packer/processing stage and on up the supply chain to the consumer. The costs and complexity of such a supply chain segregation system and/or animal ID system would be huge. Of equal importance is the fact that the COOL law requires US animals to similarly be identified as to origin of birth, origin of feeding and origin of slaughter. US product cannot satisfy the requirements of the law by default and systems to identify and track US origin product through the supply chain up to the retail meat case just do not exist. In other words, the US beef and pork industries are not at the point where compliance with the law would be possible. Therein lies the problem.

Sparks attempted to develop a set of supply chain cost estimates for the various covered products under COOL with the intent of demonstrating just how disruptive and costly the implementation of mandatory COOL would be. The results of this effort are provided in a summary fashion in **Tables 1 and 2**.

For the cattle supply chain, we broke the supply chain into four primary segments and attempted to develop verifiable cost estimates at each level of the chain. While significant costs were identified at the cow-calf/backgrounder and feedlot stages of production, the majority of the costs were identified at the packer/processor and in the retail distribution and retail store levels of the supply chain. For the beef industry, it is our opinion that total costs per head would approximate \$50.00 and this would translate into an industry aggregate cost of \$1.5-1.7 billion annually. One might argue that with cattle prices in the \$90-100/cwt. price range, maybe the industry can actually afford this level of costs. However, for a more realistic price level that tends to range from \$60-

80/cwt., such costs are prohibitive and would significantly reduce the competitiveness of the beef industry relative to pork and poultry.

Table 1: Beef Supply Chain COOL Cost Estimates (US\$)

	\$/Head	Segment Cost (Million \$)	Calculation Process
Cow-Calf Producer, Backgrounders	\$4.88	\$198.0	38 Million Head Calf Crop 2.5 Million Head Imports
Feedlot	\$3.75-5.75	\$109-\$167	29 Million Head Sold
Packer/Processor	\$15-18	\$435-522	29 Million Head Steer/Heifer
	\$4*	\$24	6 Million Head Cows/Bulls
Retail Distribution and Retail Store	\$23	\$805	8 Billion lbs. sold @ \$10/cwt from 35 Million Cattle
TOTAL	\$47.13- \$51.63	\$1,571- \$1,716	

* Not included in total per head cost

For the pork industry, a similar analysis was conducted and the results are provided in **Table 2**. Because of the vertically integrated nature of a significant component of the US hog industry, it was determined that there would be a large difference in costs for those industry participants that were integrated, as compared to those participants that were not. For integrated hog production systems that control the entire production system and are not exposed to ANY Canadian hogs, COOL compliance up through the integrators packing/processing facility would be easy to attain. The product moved into distribution could be identified to the point that it would facilitate labelling of that product as “born, raised and slaughtered” in the US. We put the cost per head at about \$.50/hog to cover certification and identification of the live animals through the back door of the packing plant. Retail and distribution costs would push integrated system costs to an estimated \$3.25/head.

Table 2: Pork Supply Chain COOL Cost Estimates (US\$)

	\$/Head	Segment Cost (Million \$)	Calculation Process
Integrated Hog Production and Packer/Processor System	\$0.50	\$12.5	25 Million Hogs per Year
Retail Distribution and Retail Store	\$2.75		
Total Integrated System	\$3.25		
Large Scale Closed Production System, Non-Integrated	\$.75	\$18.75	25 Million Head per Year
Small Independent Non-Integrated Production System	\$1.50	\$67.5	45 Million Head per Year
Non-Integrated Packer/Processor	\$2.00-6.00	\$146-\$438	73 Million Head per Year
Retail Distribution and Retail Store	\$2.75		
Total Non-Integrated System	\$5.50-10.25		
Sows and Boars	\$2.00	\$6.0	3 Million Head per Year
Retail Distribution and Retail Store		\$263	3.5 Billion lbs. sold @ 7.5 cents/lb from 95 Million Hogs
TOTAL	\$3.25-10.25	\$513.75-\$805.75	

For non-integrated hog production systems, there would be a wide range of per animal costs depending on the mix of production systems supplying the non-integrated packer. If a packer had supplier arrangements with a limited number

of hog producers whose systems could be fully certified as being US production only, supply chain costs could be expected to be moderately above those for an integrated operation. Additional costs are associated primarily with the packers need to do some segregation of slaughter and processing. For those independent packers that sourced hogs from a large number of small to medium sized producers, costs would be even higher because identification and segregation issues would be more complex. It would be these operations that would be currently killing Canadian origin isoweans or feeder pigs along with Canadian origin butcher hogs.

In summary, our analysis indicated that total per hog costs could range from about \$3.00 on the low side to as much as \$10.00 on the high side. Given the volume of hogs and pork moving through the US supply chain that would be subject to origin labelling at the retail level, the total annual industry cost was estimated to range from about \$500 million to potentially in excess of \$800 million.

Although somewhat theoretical in nature, these are the costs that the US pork system would likely face. In reality, the industry would likely change the way it operates so as to avoid or minimize these costs. One such tactic that one could envision as being easily deployed would be a “non Canadian” sourcing specification on its suppliers. Packers could force producers to certify that their total production was of US origin. This would be fine for those domestically oriented farrow to finish operations but for those mid west producers that feed out the 5-6 million head of Canadian feeders and isoweans that enter the US each year, such a condition would be very problematic.

Some packers that rely on Canadian origin hogs for their daily throughput could set up specific days or shifts for killing only Canadian hogs and while this would solve some of their problems, they would still have to be able to verify that inbound hogs were, in fact, of Canadian origin and then have the segregation capabilities to keep the Canadian origin product segregated through the packing facility and into distribution. Their retail distributors and retail customers would likewise need to maintain the segregation of the product all the way to the retail store meat case and therein lays the real costs of COOL.

■ **Conclusions**

- COOL is a short-sighted attempt by anti trade constituents in the US to construct a complex and costly trade barrier to trade in livestock and red meat
- The law would seem to have little if any economic merit and is being touted as a consumer right issue when in fact, consumers have consistently

indicated that they have no specific interest in the origin of their beef and pork

- The costs for COOL, as current voluntary rules are written, would be highest for beef but also substantial for pork
- Since poultry is exempt from COOL, the legislation would be very beneficial to the US broiler and turkey industries
- COOL would most likely result in a major adjustment in North American trade because the costs for origin segregation of livestock and products would be prohibitive
- Lack of access to Canadian cattle and hogs would create an over capacity situation in the US beef and pork packing sectors which would lead to additional consolidation of both industries
- The huge advantage that integrated operations would have over independent producers and packers suggests that those producers that this legislation was supposedly designed to help would be hurt the most
- Canada's cattle and beef industries would ultimately put in place more packer capacity to kill most of their cattle and hog production and while there would remain cost restraints on trade in fresh retail meat, the potential for expanding trade in case ready products would be huge

One can only hope that as more thought and reason is applied to COOL, changes in the mandatory aspects of the program will be successfully addressed from a legislative perspective. If consumers do want to have product identified by origin, business will accommodate and meet that need as long as the consumer has a willingness to pay the associated costs. The US already has in place certification and verification systems and protocols that would meet the needs of a voluntary origin of labelling program. They have never been implemented for this specific purpose because the consumer demand for origin labelling has never been expressed.

I appreciate the opportunity to present a US view on COOL. Since this is a very fluid situation, there will likely be many changes to report in January.