REGROWING RURAL AMERICA THROUGH VALUE-ADDED AGRICULTURE

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REGROWING RURAL AMERICA THROUGH VALUE-ADDED AGRICULTURE

TUESDAY, JULY 17, 2001

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON RURAL ENTERPRISES,
AGRICULTURE, AND TECHNOLOGY,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The Subcommittee met, pursuant to call, at 10:10 a.m., in Room 2360, Rayburn House Office Building, Hon. John R. Thune [chairman of the Subcommittee] presiding.

Chairman THUNE. Let's get this hearing this morning under way. I want to welcome our witnesses this morning and others who are interested in the subject. This is a subject that is near and dear to my heart, and today's hearing has been called to discuss how we can regrow rural America through value-added agriculture.

Agriculture is the lifeblood of many rural States' economies, and value-added enterprises will greatly aid the revitalization of rural communities. Producers want and need to reach up the agriculture marketing change and capture the profits generated from the processing of raw commodities in order to compete in an increasingly concentrated marketplace.

The family farmer is America's original small business owner, and in today's concentrated ag marketplace, producers have often been forced to accept lower prices for their commodities. This trend toward consolidation has been very pronounced during the last decade. For example, the hog industry has consolidated rapidly with the four largest firms' share of hog slaughter now reaching roughly 57 percent compared with 32 percent in 1980. In the cattle sector, the four largest beef packers account for about 79 percent of all cattle slaughtered, compared with 36 percent in 1980.

In addition, from 1984 to 1998, consumer food prices increased 3 percent, while the prices paid to farmers for their products plunged 36 percent. The average wheat farmer, for instance, earns about 3 cents on every box of Wheaties and about 5 cents on a loaf of bread.

The problem facing Congress is how to help farmers become price makers instead of price takers. To many of us, expanded opportunities for value-added enterprises are the answer.

While producers have great interest in pulling together to add value to their products, two primary barriers stand in the way. First, producers do not have the technical expertise to launch extremely complex business ventures like value-added cooperatives. Farmers are outside their arena when it comes to putting together processing plants. Second, producers are currently cash-strapped. Even if enough investment capital could be accumulated to initiate development of producer-owned value-added processing, many of the consolidated players in the market could squeeze producer-owned entities out before becoming profitable.

To help jumpstart the process, I, along with my colleagues Jo Ann Emerson of Missouri and Dennis Rehberg of Montana, have introduced two bills to assist farmers who want to create new value-added enterprises. H.R. 1093, the Value-Added Development Act for American Agriculture, provides $50 million in grant money to States to form agriculture innovation centers. The ag innovation centers would provide desperately needed technical expertise, engineering, business, research and legal services to assist producers in forming producer-owned value-added endeavors.

H.R. 1094, the Value-Added Agriculture Investment Tax Credit Act, allows producers to receive a 50 percent tax credit on investments in producer-owned value-added enterprises. The bill provides a maximum tax credit benefit of up to $30,000 per year per producer, and the tax credit may be applied over a 20–year period.

Congress needs to help provide opportunities for producers to create new value-added ventures, and these two bills are an inexpensive way to accomplish that very goal.

Again, I want to thank our witnesses for appearing before our Subcommittee this morning, and we look forward to hearing your testimony.

[Mr. Thune's statement may be found in appendix.]

Chairman THUNE. Before we begin receiving testimony from the witnesses, I do want to remind the witnesses that we would like each of you to keep your oral testimony to 5 minutes. In front of you on the table is a box, which is not lit up yet, but should be, which will let you know when your time is up. When it lights up yellow, you will have 1 minute remaining, and when 5 minutes has expired, a red light will appear. Don't worry. There is no trap door or anything there, but that should signal that you should begin wrapping up your remarks.

Our first witness today is a gentleman from my home State of South Dakota, who has a long history of involvement in agriculture and a very keen interest in this particular issue. He is Mr. Wayne Nelson, a grain farmer from Winner, South Dakota, which is out in God's country in South Dakota, west of the Missouri River, which is where I call home. And Wayne is the president of the group Communicating for Agriculture and the Self-Employed, and also is, as I happen to know from visiting with Wayne and from past history, he is an active farmer as well in the Winner area.

So we will start, Wayne, with you and welcome you to the Committee and look forward to hearing your testimony.

STATEMENT OF WAYNE NELSON, PRESIDENT, COMMUNICATING FOR AGRICULTURE AND THE SELF-EMPLOYED, WINNER, SD

Mr. NELSON. Thank you.

Chairman Thune and members of the Committee, I thank you for the opportunity to speak to you today about an issue that has long been a priority to the members of our organization, an issue that we believe is a vital part of long-term strategies for the success of rural America, how to spark the development of successful value-added agriculture enterprise.

As the Chairman said, I have a farm in western South Dakota; been farming there with my wife, Pat, for 30 years. But I also have the privilege of serving as president of Communicating for Agriculture and the Self-Employed. CA is a national nonprofit rural organization made up of farmers, ranchers and rural small business people from across the Nation. We work on a variety of legislative and public policy issues, but none are more important than the one goal of keeping rural America alive and healthy in terms of our individual farmers and our rural communities.

Mr. Chairman, we want to thank you for calling this important hearing to discuss ways to enable value-added agriculture to help farmers and build new jobs and a stronger economic base for rural communities. There are many reasons value-added agriculture development is important, but we feel the most fundamental reason is simply low farm income. This is the fourth consecutive year of drastically low farm prices. Today on my farm in South Dakota, we are preparing to harvest wheat in the next few days. The price of wheat is about 2.60 a bushel, which is about a dollar a bushel under the cost of production on my farm.

The markets have been consistently low for all the major crops. Livestock and dairy prices have swung widely, but the damage of low price periods has outweighed recent periods of recovery.

The second reason to strengthen value-added agriculture has to do with the changes under way and the structure of the farm economy. It is now abundantly clear that vertical integration in agriculture is here to stay. This is a cause of great worry to many farmers. But the results of this trend are by no means necessarily bad. Vertical integration can have many benefits. The question is, can farmers participate, and will they share in the rewards? Vertical integration from the farmer's field to the grocery shelf offers a better opportunity to better line up supply with demand. Both of these opportunities, if the new system is working right, should result in additional income for farmers in this kind of a system.

In this new farm economy, the old tools we have used to try to shore up and protect farm income simply aren't enough to do the job. We need a bigger tool box and some new tools. CA believes that it is vital that we continue to have farm income support programs. The last 4 years of low prices makes it clear the farm programs have been and will continue to play a vital role in providing a safety net for farmers.

CA also sees a need for new policies and programs involving education, oversight, and regulation of contracting. We also see a need for stronger Federal antitrust oversight and an effort to preserve competition in agricultural markets and supply chains.

We commend the Chairman and others for introducing H.R. 1526, the Agriculture Competition Enhancement Act, which would put limits on mergers to prevent excessive concentration. We also believe that one of the best ways to address vertical integration is to find ways for farmers to participate as equity holders of value-added enterprises, both cooperatives and through various joint ventures.

We don't want the landscape of rural America to look like a few giant farms and a few giant corporate processing facilities located hundreds of miles away in large cities. We like the present mix of family farms, and would like to see processing facilities located in rural communities providing more jobs and income.

In my home State of South Dakota, we have an example in a small town in eastern South Dakota. Farmers are operating their own soybean processing facility that has created a better market and a better price for their product.

We think there are some new tools that would also help. We offer our support and encouragement to approve H.R. 1094, the Farmers Value-Added Agriculture Investment Tax Credit Act. As you know, this bill calls for showing—allowing producers to receive a 50 percent tax credit on investments and producer-owned value-added enterprises. The tax credit could be for up to $30,000 a year and applied for over 20 years.

Additionally, the companion bill, H.R. 1093, calls for USDA to administer grants that would go for establishing innovation centers to provide technical assistance, market and business development services for the new value-added ventures. These are good legislative proposals.

We also believe that it is important for us to find ways for new beginning farmers to get started in agriculture and to participate in value-added agricultural enterprises. CA would like to see enacted a bill that would exempt State Aggie Bond loan programs from the overall bond cap. This proposal is included in H.R. 2347, introduced by Representative Nussle, that is the TERFF Act, the same ag package that was introduced by Senator Grassley in the Senate a couple of months ago. We would also like to see a legislation develop that would allow the Farm Service Agency loan guarantee to be used on Aggie Bond loans. We support the entire H.R. 2347, the entire TERFF package, which has some very good ag tax incentives to help both farmers and the rural communities that the farmers serve.

In summary, CA believes we need new additional tools in the agricultural policy tool box to put our family agricultural system back on sound footing. Value-added agriculture is not a panacea, but is one of the more important strategies that we need to pursue more seriously than we have in the past.

We have all talked a good story about value-added agriculture and the need for farmer participation for many years now, but the truth is we have not—it has not been an easy goal to achieve, and we need to work harder at trying to achieve this goal.

Thank you very much, Mr. Chairman.

Chairman THUNE. Thank you, Mr. Nelson.

[Mr. Nelson's statement may be found in appendix.]

Chairman THUNE. And I neglected to mention earlier, and I should have, the gentleman from Pennsylvania, Mr. Shuster, is with us, and we have now been joined by Ms. Moore Capito from West Virginia and the Ranking Member of this Committee, Mr. Udall from New Mexico.

And I would like to open up if anyone would like to make any opening remarks, or we can proceed with the witnesses. Anybody have a comment?

Mrs. CAPITO. No.

Mr. UDALL. I would just ask that my opening statement be put in the record so we can get directly to the witnesses, Chairman Thune.

Chairman THUNE. Very good.

[Mr. Udall's statement may be found in appendix.]

Chairman THUNE. I appreciate your comments, Mr. Nelson, and we will now turn to Ms. Terry Jorde, who is president and CEO of the Country Bank, USA, Cando, North Dakota. Ms. Jorde is also a member of the Independent Community Bankers of America, which represents a lot of the small community and independent banks in rural areas of the country, places like many of us represent here this morning.

So we welcome you to the panel and look forward to your testimony.

STATEMENT OF TERRY JORDE, PRESIDENT AND CEO, COUNTRY BANK, USA, CANDO, ND

Ms. JORDE. Thank you, Chairman Thune and members of the Committee. And thank you for holding this important hearing. As you said, my name is Terry Jorde, and I am on ICBA's Agricultural-Rural America Committee and president and CEO of Country Bank, USA. Our agricultural bank is located in the small community of Cando, a town of about 1,300 people in Towner County, North Dakota. I have lived in Cando for 22 years, and I am married to a potato farmer.

Over three-fourths of the community bank members of the Independent Community Bankers of America are located in communities of under 20,000 people; 86 percent are in communities of less than 50,000. Our membership has a strong interest in ways to help rural communities diversify and add value to ag commodities. Our bank has tried to be a catalyst for rural development and has worked hard over the past decade to create new jobs.

Cando established an economic development group called the Durum Triangle Development Corporation back in 1978. That organization has now evolved into a countywide development corporation whose nine-member board consists of two community bankers and an attorney, our hospital administrator, a city council member, a county commissioner and various other people from our county. This group, along with two local banks in Cando, financed the first totally integrated pasta plant in the Nation.

About 20 years ago very little durum wheat was milled in North Dakota. Now, well over 10 percent of all U.S.-produced durum is being milled there. Pasta plants such as this one have created over 500 jobs in my local area.

Our bank has also helped originate a loan to a local foundry that casts small agricultural implement parts. We were able to convince a Canadian foundry owner to locate an American plant in Cando. We brought lots of people together with various types of expertise, a couple of bankers, an attorney, a State legislative representative and the president of the local electrical cooperative. We worked together to create a financial package utilizing State and Federal programs, an example of community involvement, to attract new business ventures. This business opened in 1995 and now has about 90 employees.

Let me suggest four basic principals for rural development through value-added initiatives. Number 1, target resources to rural communities based first on population. Number 2, provide tools to complement, not compete with, the private sector. Number 3, target resources to various sizes of businesses, including individuals. And, number 4, maintain the population infrastructure.

First we must target resources to rural communities. Given a choice, new business will always locate in urban areas unless given an incentive to do otherwise. The labor pool is larger, and the risks are lower. But we do need to create new jobs in rural areas if we are to survive. This implies a population-based criteria such as the business and industry programs required that loans go to communities of 50,000 or less.

Targeting rural areas provides off-farm jobs, maintains the local tax base, maintains population which can keep local leadership in a skilled work force, and maintains the infrastructure and services needed to sustain economic life.

Second, we should complement efforts of the private sector. Rural bankers are keenly aware that the future of their locally owned institutions are directly tied to the future of their rural communities. With thousands of small banks in rural areas, there is a vast network already available to act as catalyst to bring together people and leverage resources to attract new business opportunities.

Greater use of guaranteed loan programs would be one obvious tool. Small bankers can also participate in larger loans, especially if they have guarantees.

Third, let's not forget about individual entrepreneurs. For example, one of my customers is a farmer who started a business that uses flax straw to make 20-foot erosion control logs that are shipped all over the country to minimize erosion after flooding and forest fires. He is further expanding his business to make hanging flower basket liners for horticultural use.

He bought a closed schoolhouse for $1 for the manufacturing site, and our bank has helped to fund this value-added project with the help of an SBA 7(a) guaranteed loan. My point is that he began as just one individual entrepreneur.

Finally, we must maintain population and infrastructure. The 2000 census revealed that in the 1990s, 676 counties, primarily rural agricultural counties, lost population. Despite the efforts in my county, we lost nearly 21 percent of our population. At some point populations can fall below a critical mass, meaning the community is headed for an irreversible decline because they lack the human resources needed to remain viable.

ICBA welcomes your legislative efforts to help producers capture more from their raw products through value-added processing. H.R. 1093 provides grants to create special innovation centers to provide much needed technological expertise to assist producers in forming their own value-added business. H.R. 1094 provides a tax credit for investments by farmers in value-added businesses. Farmers, like everyone else in rural America, are limited in amounts that they can invest. Such proposals have merit, especially if they are targeted to the rural communities. Congress should consider combinations of tax credits, grants and loan guarantees in ways that can ensure community bank participation.

Mr. Chairman, there are other suggestions in my written statement for tax incentives and real development initiatives such as Subchapter (S) reform for community banks, greater use of ethanol, increased deposit insurance and index it to inflation. It is a source of funding for the community, but hasn't been raised since 1980, eroding its real value in half.

Increase funding for USDA's Business and Industry Guaranteed Loan Program. Last year almost 400 projects could not be approved due to lack of funding.

Limit or eliminate fees on guaranteed loan programs in rural areas. The administration's budget for both USDA's B&I Guaranteed Loan Program and SBA loan programs recommend new fees. To deal with some of these budgeting issues on a more permanent basis, we suggest that Congress pass legislation prohibiting USDA and SBA from raising loan fees without Congress's approval, and establish a large pilot program that would eliminate fees on small business loans in rural areas. Eliminating fees would attract greater participation and enhance the strength of the portfolio. If fees are too high, only high-risk ventures will seek financing through SBA, thus increasing SBA's potential for losses.

We need greater broadband access in rural areas. And again, we also agree that we need to enhance the Aggie Bond Program.

And finally, Mr. Chairman, rural America has a critical need for equity capital. The Center for the Study of Rural America recently explored the issue of attracting equity capital to rural areas. They concluded that few companies with high growth potential are located in rural areas. Urban areas can attract equity capital much more efficiently than rural areas. Creating local wealth that is locally controlled should be an essential goal, and a double bottom line is needed, both a good rate of return, but also providing the rural communities with a major economic boost, like jobs.

Any serious attempt to boost the supply of equity capital has to include banks. The ICBA has worked with the Coalition on Legislation to create a rural equity fund to help spur business development in rural communities. The equity fund would encourage private investments and value-added agricultural enterprises and small business start-up and expansion. A healthy rural community obviously needs many types of rural businesses. Unfortunately, large venture capital funds are not interested in focusing on rural America. There is plenty of venture capital for Silicon Valley, but not much for the Red River Valley.

Mr. Chairman, I thank you for the opportunity to participate, and we look forward to working with this Committee. I would be happy to answer any questions.

CHAIRMAN THUNE. Thank you, Ms. Jorde.

[Ms. Jorde's statement may be found in appendix.]

Chairman THUNE. And we next will hear from Mr. David Reis, who is the president-elect of the Illinois Pork Producers Association. Mr. Reis farms and lives in Willow Hill, Illinois. Mr. Reis.

STATEMENT OF DAVID REIS, PRESIDENT-ELECT, ILLINOIS PORK PRODUCERS ASSOCIATION, WILLOW HILL, IL

Mr. REIS. Thank you.

Chairman Thune and members of the Committee, as you said, my name is David Reis. I am a pork producer and a fifth-generation family farmer from Ste. Marie. I am currently serving as president-elect of the Illinois Pork Producers Association, and it is an honor to appear here today before the Subcommittee on behalf of the over 240 members who are independent pork producers that make up our newly formed cooperative to share with you some thoughts of what we were trying to accomplish in this ever-changing agricultural industry.

As has been said before, like many industries in this country, agriculture is truly going through a period of extensive change and consolidation. The result is the family farm is giving way to a system of contracted and integrated corporate operations. While some producers and organizational groups have resorted to spending their time and resources trying to stop this trend, we at American Premium Foods have chosen to be proactive and engage in activities that will allow us to not only control our own destinies, but also to create more jobs and preserve rural economic activity as well.

In our industry, the only way for family farms to survive this consolidation is for them to coordinate and capture the profits from processing their current commodity, live hogs, into value-added food products. We must stop selling hogs and begin marketing pork.

American Premium Foods Co-op was organized in late 1999 after a year of business plan development and membership recruitment. We plan to construct a pork packing and fresh processing facility that is producer—wholly producer-owned. The plant will be capable of handling 2,800 head per day on a single-shift basis. Each carcass will be individually tracked through the plant, and producer members will be paid for the wholesale value of the primal cuts for their hogs. The profits from additional processing will be paid to them, individual members, according to the producer's percentage ownership in the plant. Our $30 million facility will employ 210 people and have an annual payroll of approximately $6 million.

We have, during the course of this project, received a lot of support from various State agencies and groups wanting us to get up and go, and we really don't have a business model to follow in the United States, producer-owned cooperative. There are some smaller ones, but none of this size. Department of Commerce and Community Affairs, Department of Ag, even the State of Illinois issued us a $1.7 million grant to help us with our start-up costs, and just a couple of weeks ago we found out that we were awarded a $500,000 grant from the USDA through their Value-Added Agricultural Product Market Development Program that was new last year.

Our project, however, hasn't been without its fair share of frustrations and attacks from the industry critics, because we are the first venture of this size. We had no business plan to model. We were deemed high-risk start-up. We were even told by some people to be aware of snake oil salesmen; that this project, a project of this size, just couldn't be put together by farmers.

You have heard it mentioned here before that most of the producers' equity and ability to invest in such a project was wiped out with the 8-cent hogs in 1998.

As you can tell, it was easy for people to sit back and give us reasons why we couldn't do this, but our group of directors and the leadership has held its course for 2½ years now. We believe that what we are trying to do is worth fighting for because we feel what is at stake is our independent operations. And everyone from the local extension office to the commodity groups to the halls of Congress are promoting value-added. And I can tell you it is not that easy, that these projects just don't happen overnight. But the longer it takes to get these things up and going, the more consolidation continues.

It was just announced a few weeks ago that Seaboard Corporation was scrapping their plans to build a new plant in Kansas, which further backs up our beliefs that the only way that increased growth in the packing industry is being incurred is by acquisitions and mergers. They are coming into the smaller plants, the bigger packers, and buying them. So they are really not increasing shackle space, they are just buying up other plants. And we have all seen in recent weeks with the high cost of gasoline and fuel what happens to an industry when they quit investing in itself. And it is a major problem with the shackle spaces that are available in the pork and beef industry.

So what can Congress do to help? We need common-sense solutions and assistance if more projects such as ours are going to successfully maneuver through the critical period of planning and start up. Whether it is beef or pork packing plants, soybean crushing, ethanol, wheat, aquaculture or one of the other value-added concepts being discussed, oftentimes the difference between success and failure is the amount of time and money spent doing the preliminary work. These ventures need assistance in hiring the best firms to conduct the feasibility studies, legal representation, engineering, marketing, business plan development and so on.

We in the pork industry in America know how to raise pork better and more efficiently than anyone in the world, but we need a little boost when it comes to becoming better business owners in a broader sense when it comes to a project this size. That is why we are so excited about Congressman Thune's value-added agricultural package. In fact, when I heard about it from Brad, I almost leaped out of my chair because I testified a month ago, and two of the things they suggested was a tax credit bill and block grants to States. So this is common-sense legislation, and I hope we can move it forward.

We feel that both 1093 and 1094 will address two major hurdles that co-ops face as they develop from the initial vision stages all the way to becoming profitable ventures for their members. With 1093, I can't explain how many dead-end roads we went down, programs we found out that were available after the fact, just how many ideas and support from people we could have got if there was a State-run co-op development center in place. They need to be State-run because they need to be relatively close. There is a couple in Missouri, but, you know, we are all on shoestring budgets, and sometimes you have got to visit these offices several times a month.

And if every State had one that was local, the producer could go there. There are also a lot of rules and programs that are just different in each State.

So in May of this year, the Illinois Legislature passed a bill that creates the first AgriFirst Program, and its ultimate goal is to become a DECA-like program that can help fund and do things for agriculture. But up front it is just going to be a program where it can be the incubator center for knowledge and business plan development and so forth. So this would tie in great with that. Illinois could apply for one of these grants, and it would help them fund their program at a much higher rate.

With regards to 1094, some say that the tax credits are always a longshot. Sometimes I think that they don't work hard enough on them. But this puts incentives where they do the most good in established projects that have come to fruition and will enable the participating members to recover more quickly their initial capital investments, which in turn make the co-op more profitable, which in turn allows the members to reinvest their money back through their communities, and this is why we are here today.

I really encourage Congress to push for these tax credits. I know it has got to go through another Committee, Ways and Means, but these are both excellent bills, and I think most of the commodity groups, if not all of them, are going to be behind them.

I am running short on time. But from the Small Business Administration I think Terry pointed out a lot of things. The fees and the application process makes a lot of these unavailable to ag projects this size, a lot of $150,000 loans and such, and we are doing a $30 million project. So perhaps the Small Business Administration could do a better job of cross-selling their programs. If we go in and ask for what is available, maybe they could say, go to this one, or go to that one. Sometimes I think they just say, well, this is what we got, and that is it.

In closing, Mr. Chairman and members of the Committee, the producers that are in our particular co-op have agreed to lay their operations on the line and invest what little capital they have left into this project. Two years of holding the membership together, a project that hasn't been built yet really says a lot about eight hogs. They have hung in there, and they have hung in with the board of directors. We should be finishing up financing this summer, and hopefully we will start this fall. But the future of the independent pork producers are hinging on our success. They are a key ingredient to the sustainability of the landscape. They eat corn, they eat soybeans. And our industry is changing rapidly. And if we can work with Congress collectively, maybe we can come up with ideas, common-sense ways to preserve the livelihood of the pork producers throughout the Midwest.

Thank you, Mr. Chairman, and I would be happy to answer any questions as well.

Chairman THUNE. Thank you, Mr. Reis.

[Mr. Reis's statement may be found in the appendix.]

Chairman THUNE. We will get to questions in just a moment, but our final witness this morning is Mr. Jay Truitt, who is executive director for legislative affairs for the National Cattlemen's Beef Association.

Mr. Truitt, it is good to have you here this morning, and please proceed.

STATEMENT OF JAY TRUITT, EXECUTIVE DIRECTOR FOR LEGISLATIVE AFFAIRS, NATIONAL CATTLEMEN'S BEEF ASSOCIATION

Mr. TRUITT. Thank you. And, again, Mr. Chairman and members of the Committee, we thank you for the opportunity to be able to speak to you today.

Again, I am here today on behalf of the National Cattlemen's Beef Association, which is the trade association that represents America's cattle farmers and ranchers and is also the marketing organization for much of what takes place in the beef industry. We are proud to be the leader in the Nation's food and fiber system. Beef is the largest segment of agriculture, and, again, we are proud of that. It is something that we are pleased with.

We, too, have gone through dramatic changes. We feel that our rule as an initial organization is to begin to lay the groundwork so that the legislation, as it is before the Committee today and has been before this Committee in the past, has an opportunity really to work.

The beef industry, not unlike the pork industry, has seen a dramatic shift and a dramatic change in the respect that I would like to talk about this morning. And what has been of key interest to us was our constant and ever-present decline in market share that had gone on for about 20 years. We realized that we were in trouble a number of years ago and began to do some strategic planning and really get focused on where that was going to change and how we could turn those numbers around. A little bit later I think I can explain why we have turned those numbers around, and we are beginning to see beef demand increase and have continued to see that increase for the last several months.

Seventy percent of the total U.S. Beef volume that moves through the marketplace is moved through the retail outlet. Over the past several years that has been a pretty consistent number. We are beginning to see some changes there, though, and how that beef moves through those retail outlets has taken some dramatic changes.

We look at beef consumption numbers in the United States, and not to slight my friends from the pork industry, but we are still number 1. We are proud of that. We like to point that out again, as I said earlier. But at 66.2 pounds per person per year, we know that there is a huge marketplace out there now, and, again, we hope that that number will continue to increase.

We started laying the groundwork in the mid-1980s and really got focused late in the 1990s at NCBA in trying to figure out ways that we could make products more usable for consumption, and also that we could begin to develop some of the technology and discover many, many technologies. That made it possible for anyone, from producers that form together in a small marketing organization all the way up to the largest members of our industry, to be able to move into the next generation of retail consumption, which we believe is beginning to arrive.

Just 3 years ago, heat-and-serve entrees were something that probably no one really thought about a whole lot. Today it has become a huge business for us, and the convenience section in the fresh meat case, which was zero again just a few years ago, is now $117 million. That is something that we are very proud of, and it has been a great success story.

When you look at some of those individual successes involved in creating those products and developing those products, what we find is that the incentives that were put in place, in some part because of NCBA's use of check-off dollars, to run contests and promotions that help reward people that were creative and looked for solutions in the retail outlet, but also producers that took the technology that we had found through our research and development programs and were able to apply them at whatever scale was appropriate and really become extremely successful—and there are a number of cases where we have seen heat-and-serve products now that are in the marketplace that started in someone's kitchen, and we are as proud of that as we can possibly be, and we think it is a huge part of the future of the beef industry. And, again, we see our role in making sure that they have some the basic technical and physical tools that are needed in some cases to make sure that we can move in that direction.

New products, again, are those promotion programs, and those research projects have been funded by our check-off dollars that producers across this Nation contribute in. NCBA mentions those dollars for the Cattlemen's Beef Board, which is a hundred-plus-member board designated by the Secretary to administer that program, and we are very pleased with the effect that that has had on our industry. We think that that is one of the key reasons why now for eight quarters in a row beef demand has been increasing, and in large part it is because of these new product areas that have moved in and began to take up space in the retail counter in a positive way, from our perspective.

Category management tools and the mechanisms that will allow us to actually move into the marketplace have become a key component in the way that we have redesigned the marketing of products that allow producers to find the space where they fit in the retail outlet. We think that is essential.

Again, in closing, we would to say that—and I spent a great deal of time working with Mr. Talent. I spent a lot of years in Missouri and on the ground working with him on these programs.

I notice that all of you have been very focused on trying to address the needs of producers, and in some respect probably consumers as well, but rural communities around the country, and I think we are on the right track. And I myself am a participant in a couple of new-generation cooperatives. My family has been in the cattle business for a couple of hundred years or more now, and we see it as the way that we continue to remain engaged and maintain some of the profitability.

I have a lot of respect for the gentleman to my right because I realize after being one of the latecomers exactly how much work goes into these projects, and any assistance that you can provide to that process, whether it be in technical information, expertise or just general aid, is obviously helpful.

On the tax and credit issue related to the legislation, obviously, it is a huge investment, and from a producer's standpoint, it is an investment that probably means that there will have to be sacrifices made. Any way to lessen the pain of that investment is obviously a step in the right direction.

And again, we commend you, and, Mr. Chairman, thank you for this opportunity to address the Subcommittee. We thank you very much for all the hard work that you do, and I would be happy to answer any questions as well. Thank you.

Chairman THUNE. Thank you, Mr. Truitt.

[Mr. Truitt's statement may be found in appendix.]

Chairman THUNE. And thank you to all the panelists for your excellent testimony, and just a couple of things that—one observation, and that is, Mr. Nelson, you refer in your testimony to something that I think is important in this, too, and that is that we have seen this increasing level of concentration within the agribusiness sector, and, frankly, I think we need some—a new look at antitrust legislation in that area, the bill that you referenced, the bill that I introduced changing the level of scrutiny that we apply to agriculture mergers and really forces us for the first time to focus on the impact on prices paid to producers, which is something it hasn't been a part of.

And so I say that, realizing that that is probably a more difficult thing to get done, but I also think that it is very important for this Congress to begin to look with a higher level of intensity at what is happening in the marketplace out there and the impact it is having as you see this increasing level of concentration. But that is something that obviously we are going to have to build support for out here, and changing antitrust law is no easy feat.

In the meantime, we do, I think, have to take as much control of our destiny as we can in the industry of agriculture, looking at ways that we can reach up the ag marketing chain and capture more of the value of the products, the commodities that we grow in rural areas. And, Mr. Reis, you had mentioned that we have got to quit selling live hogs and start marketing pork, and that really is—and, Mr. Truitt, you alluded to that as well, that those are all things you have got to start thinking about, what your market is out there, and how do we come up with ways of meeting those demands in that marketplace and processing and adding value to the things that we grow in rural areas.

So it is a very timely subject, one which I think we, again, need to look at as a Congress, as policymakers, as to what we can do as policymakers to provide that kind of activity.

Just a couple of questions. One—I guess I think you mentioned in your testimony—a couple of you did make reference to the SBA loan programs. And I guess my question would be how beneficial are the SBA loan programs to rural America? If they are not, how can they be improved? And I think, Mr. Reis, you had noted in your testimony that in some cases SBA loan programs aren't designed for projects as large as yours, and yet, Ms. Jorde, you had mentioned that some of these programs need to be targeted to smaller-type operations and types of projects. And so there is—I mean, there are kind of conflicting points of view about how the SBA programs are currently designed, how they work, and so if any of you would care to comment on that, I would appreciate hearing that.

Mr. REIS. I think the program is designed for situations that she gave examples of. If I want to market my meat, and there is a particular individual doing this in Illinois, he would qualify for loans such as that. So I think that the language or the rules that are in the administration do work for that. But when we come in and say, okay, we have got a $30 million project, and we have got 6, 8, 10 million of it is investment capital from the producer, and we want to get a loan guarantee or we want to get money for the rest of it, the Small Business Administration just—it doesn't handle programs as large as that, projects.

Chairman THUNE. Ms. Jorde, would you care to comment?

Ms. JORDE. Yes, I would agree. And I understand the importance of what he is talking about. My comments were probably more related to some of the real development needs that we have. In some cases we have been able to use small business loans or Small Business Administration guaranteed loans for value-added projects. In the case that I alluded to with the one individual, that certainly worked. We are working on a financing package with another cooperative that also is a pasta plant where the dollar amounts aren't 30 million. They are closer to a million or 2 million, and we are looking at the SBA 504 program for that program.

So I think SBA does have a lot of use still in rural America, but over the last several years we have seen increasing fees not only up front, but also on an ongoing basis. We pay a half a percent to the SBA on every loan that we have every month, so that increases the cost of providing the credit to the borrower. It increases their fees up front, and ultimately what happens is that the borrower that is able to get financed elsewhere without SBA will go there, and so you end up with an SBA loan portfolio that has the higher-risk loans in it, which defeats the purpose of the strong SBA program. It is one of those things where if we can make it up in volume and lower the fees, but have more participants, I believe we would have a stronger program.

Chairman THUNE. You mentioned, too—how does the USDA B&I Program, Business and Industry Program, how has that been beneficial in targeting rural areas? I mean, is that something that, again, could be—is there room for improvement there?

Ms. JORDE. Well, I think there is. I think it is a beneficial program. I think sometimes the USDA program isn't as efficiently administered, at least in my neck of the woods, as SBA is. I have heard that from other bankers. But also it appears to be targeted more toward the large businesses; quite a bit more paperwork, a longer processing time, and then generally it runs short of money. As I indicated, I think there were several hundred projects that weren't able to be funded last year because it ran short of funding. But I definitely feel that it is a very valuable program that needs to be enhanced.

Chairman THUNE. Are these—go ahead, Wayne. I am sorry.

Mr. NELSON. No. Quickly. I think that these ag innovation centers in the States could act as a clearinghouse so, as was said earlier, they could understand many of these programs, the SBA, the B&I, and possibly some other ones that aren't even known to farmers and to people starting these co-ops or joint ventures. The ag innovation centers would help very much if the State——

Chairman THUNE. Does—and I should know the answer to this, but does SBA—can you, with their guaranteed loan program, make loans to cooperative-type ventures?

Ms. JORDE. Yes. I don't think there is any reason you can't. The dollar limit is the problem you run into. I believe a million dollar guarantee is the maximum on a 2 million dollar loan. A million-dollar guarantee is the maximum level.

Chairman THUNE. Okay. Let me just ask a little bit of a different question, too, and this might—if you look more to value-added ventures that are designed primarily for the U.S. Market, how important are overseas markets, and how important is the whole trade issue in trying to pursue additional types of value-added opportunities? I mean, a lot of things that we are talking about are sort of designed for the domestic market. But how important is it that we have a—you know, a free trade policy that enables us to reach some of those arguments? Would anybody care to comment on that? Mr. Truitt.

Mr. TRUITT. I would comment from the perspective that, number 1, the beef carcass just doesn't flow through the system in the way that maybe that we would like for it to, and there are certain pieces of that product that hit the retail channels that don't find their way into the U.S. Market very easily. Again, that—the reason for a lot of the innovation that we have done has been to take the chuck and the round part of our product and really find creative ways to move it into the marketplace. But in that light, as you well know, Mr. Chairman, we have continued to increase the total dollars in exports that we have of beef out of this country for some time, and that means that we send some of the higher-priced and higher-quality and, frankly, in some cases, probably the higher-margin pieces into other marketplaces that this market just won't bear. And it allows us to do some of the innovation that we do.

It—for us it is essential, and the fact that we have to be able to move certain products out of this marketplace to keep from almost drowning in them here inside this country. If we have had a primary drag on our overall profitability over the 20–year decline that I discussed earlier in our demand, it was the fact that people around the country on Saturdays and Sundays quit having pot roast. They just forgot how to cook them. And my wife is great at accomplishing that task, but I realize that she is in the vast minority, and my daughter probably is in the generation that will not cook them at all unless they come in a real easy-to-use container.

So we have changed some of those dynamics, but it is essential for us to have a marketplace that can take the products either that we don't use or that have a higher profit margin somewhere else in order to keep our footing stable.

Mr. NELSON. Mr. Chairman, two things, I think. First of all is that American producers are terribly productive, I mean just enormously productive, and as much as we want value-added success in the future, it is not going to be our total answer to take care of all our production in the U.S. So trade is essentially important with bulk commodities that are going to have to continue to be exported.

Secondly, I think there are some very keen export markets in the case of pork. I will give an example. Denmark has a slaughter facility that only is for the Japanese market. They have a different slaughter facility that is for the English market. So they actually have different cuts of pork in different facilities to go to the different export markets, and I think that is something, just as an example, that we have a great deal of opportunity in America to be able to use that with exports with value-added products.

Ms. JORDE. Mr. Chairman, I think there are challenges on the import side of the equation, too. One of the most successful value-added cooperatives in North Dakota started about 6, 7 years ago, Dakota Growers Pasta Company, and it is a farmer-owned cooperative. Many of the farmers in my area invested in this cooperative. The general manager is actually on the board of my local community bank as is—another board member on my bank board. They started out very strong, and they made a promise to their farmer owners that they would only use their durum, durum produced in North Dakota preferably, or in the United States. But they found themselves at a competitive disadvantage with other competitors in the U.S. because their competitors were purchasing durum from outside the country, from Canada, at lower costs than what our producers were able to sell it for, and that created some very big challenges for them.

So when you look at our markets, it is worldwide. Trade is extremely important, and it still does come down to being able to be competitive with the cost of that raw commodity as well. Through a very controversial decision at their stockholders' meeting—they are now allowing Canadian farmer investors to purchase shares in their cooperative in order to try to be competitive with other pasta producers in the country.

Chairman THUNE. Well, as much as I appreciate all the value-added products, I do yearn for the days of pot roast and apple pie, too.

Mr. Udall.

Mr. UDALL [presiding]. Thank you very much. Chairman Thune, I also yearn for those days.

Let me just say at the outset that I think these two pieces of legislation that we are having a hearing on here, the Value-Added Development Act for American Agriculture, H.R. 1093, and the Farmers Value-Added Agriculture Incentive Tax Credit Act, H.R. 1094, I think are very good pieces of legislation, and I would note that I have signed on, and I believe very much in trying to do everything we can to move these along.

Ms. Jorde, you mentioned about the role of the SBA in terms of possibly assisting—the administration has—and I sit on the Small Business Committee—has proposed that we have a 43 percent cut in the SBA and then adding fees on top of many of those programs. Could you or any of the other panelists comment on the impact it might have in this area?

Ms. JORDE. Well, I think it would devastate the program. I think that if you look at the numbers that the volume of SBA-guaranteed loans declined when the fees were increased in the last few years. And so I think increasing fees will just contribute to a smaller SBA portfolio, and a higher-risk SBA portfolio, because only those loans that can be funded with a guarantee, those that are desperate for the loan and will pay whatever it takes, will come into the program, and the other loans will go elsewhere.

There is a very competitive banking market out there right now, and, you know, I think we are better off, like I said earlier, to have a larger SBA portfolio of guaranteed loans with good, strong credits than limited to a few number that are willing or can only get in the program with higher fees.

Mr. UDALL. Any other comments from any of the other panelists on that?

Mr. NELSON. There is a real lot of rural small business people that use SBA loans that might not even be valued added, and we see the same comments there. Especially concerning some of the smaller loans in some of our smaller rural communities, the fees can be very much detrimental and not allow them to receive the funds.

Ms. JORDE. If I could just follow up, too, I had a conversation a year or so ago with a woman who heads up our regional area. I guess she is out of South Dakota, and I don't recall her name, but she is with SBA, and at that time they were looking into lowering some of the fees, which they did do recently. She said that their evidence shows that the loss ratio in rural areas is much lower than it is in the more urban areas and that there is a very good case to be presented for lowering fees for rural areas. So we think that this would be an excellent pilot project to look at, to see if by lowering fees, if we don't increase the volume in the portfolio, make it a stronger program while enhancing rural development.

Mr. UDALL. Mr. Truitt, you are nodding your head, so I want to give you a chance to say something.

Mr. TRUITT. I would be remiss if I didn't say we thought that lowering fees was a very good idea, especially in rural areas. And obviously there is a very real challenge for producers to manage the different investment strategies that it takes to stay in business today, with slim margins and, again, trying to make additional investments elsewhere. It gets pretty complicated. I would say that there are a number of State-based programs in a number of States that are pretty creative, and there probably are some good solutions out there to help us address some of those needs. But, again, I guess I was nodding my head to the fact we can reduce the fees associated with the loan. I know my members support that.

Mr. UDALL. Thank you. Chairman Thune mentioned the concentration of the markets in the areas that you work in, and I know in my home State of New Mexico, whenever I talk to farmers or producers, they talk about the concentrated markets—and they don't say it quite like that—but the pressures on their prices and the fact that the producers aren't getting the prices that they think they deserve. And he mentioned antitrust as one way of dealing with that, and possibly better enforcement of antitrust laws and changing antitrust laws.

Can you think of any other ways to deal with this issue of concentration of the markets and trying to get producers to get a fairer share of the whole pie in terms of production?

Mr. TRUITT. Yes, sir. I would comment from the perspective of the beef industry, I mean, I think we have already begun to answer some of those questions. And Mr. Thune had mentioned that we have four processors in the United States that control the vast majority of the livestock that go into the marketing system. But the fact is that that number four processor, their primary business is doing business with producer-owned cooperatives and cooperative marketing agreements that move through that plant or through their facilities. And at some point in the future, I would expect that the producers will wholly own that entity, and I think that is something we can look forward to seeing more and more that will happen in the future. When we look at the real growth that has taken place in our industry—and, again, I don't mean to sideline the concentration aspects of your question. But the real growth that is taking place and tremendous growth that is taking place is from some smaller and mid-range processors that have figured out how to move into shelf-ready or case-ready or fully-cooked, ready-to-serve products, or found niches within some of the other entities or niches in our marketplace. And the growth in those segments is tremendous.

I do believe that we should continually keep a close watch on what happens with our industry and make sure that the right things are happening to the right people and that everybody is playing with as many of their cards above the table as we possibly can. But we are seeing some changes take place in the beef industry that I don't think any of us could have predicted 3 or 4 years ago. Maybe high prices are helping us make those decisions, but we are in a bright spot right now and are proud of what we have accomplished.

Mr. UDALL. Mr. Reis.

Mr. REIS. With respect to the consolidation and the whole industry, and you, too, have a big thing here to deal with, you know; how do you regulate success? You look at catsup, you look at chewing gum, the market share that the two big companies have—and we are nowhere near that—but it is frustrating to farmers because of regional concentration. I can't haul my grain to Nebraska or South Dakota. The trucking costs prohibit me from going more than 90 miles.

So you have to look at who is commanding the most market in these areas, and when you really break it down like that, there is even more consolidation; so that is one thing. And you have to look at consolidation, because we haven't made money for so long, or the profits and margins have been dwindling, the concentration in the equipment—the water, the building equipment, the equipment to put out the crops. I mean, there are less and less choices there. So the farmers give up because the dealerships are closing and things like that.

So you have got a big thing here, and one of the things that sparked us to do what we did and has kept our group together is that we know that fighting concentrations is a slow process and we want to go in there and find a niche.

You mentioned the international markets. While we are not going to go after those right away, we feel that the strict European standards are going to come to America, and we want our plant to be there. We are not going to go up against ConAgra or IBP or

Smithfield. We want to find a niche that they aren't filling and try to fill that up.

The last thing with concentration, what drives it is regulations—the HACCP requirements on these plants. A lot of these small plants are closing up. They have got HACCP requirements for the killing of the animal and they have got HACCP requirements for processing of the animal. They are saying we are no longer going to kill this animal. We want to buy boxed bones and combo'd meats so we can further process it. American Premium Foods, will you kill our animals for us?

So I mean, the undue regulations put on the packing industry, and I am sure other industries can talk about that, is driving the consolidation as well.

Mr. UDALL. Mr. Nelson.

Mr. NELSON. Thank you. I think that looking at the Department of Justice, we have already made some inroads in that we have a higher visibility now over the last 2 or 3 years in the Department; but, as Chairman Thune said, it is very difficult to enact legislation because the legislation on antitrust affects not just agriculture but everything, and so it becomes more difficult. But within the departments, within USDA and the Department of Justice, I think we can continue to try to raise the bar of understanding to show them what is happening and how important it is to recognize that they might have ways already on the books to be able to help us in the concentration.

Secondly, the point that farmers need to share in this vertical integration I think is so important, and what Jay and David have said, is that in the beef and pork industry they are doing that through cooperatives or joint ventures. And the way they are doing that is by being able to have a product that the American people or the whole-world consumer wants, having that niche to where they have the product designed to what they want. And I think that is something that has happened in the past and it is continuing to happen in the future, and not just in meat but also in grains, and I think that will help a great deal with the concentration problem.

Mr. UDALL. Terry.

Ms. JORDE. Concentration is an important issue and very difficult to legislate. The Independent Community Bankers Association was formed to help—not prevent concentration, but allow community banks to stay independent and provide resources so they could do that. I think with anything like this, though, we have to be very careful on how we legislate. For example, there is legislation in place that determines whether banks can merge. There is a formula called the Herfindahl-Hirschman index that is used to determine concentration ratios before and after a merger of two banks, and in some cases what this has resulted in is in a community, say, of maybe 500 people where there are two community banks, when the one bank tries to buy the other bank because the town can no longer support two banks, it fails the concentration test of this index, and therefore the merger is not allowed; yet a large out-of-State holding bank can come in and buy up that bank and, you know, ultimately they end up losing the community ownership of that bank in that town.

So, with anything, I think we have to be careful on how we legislate and look to all the ramifications that can come as a result of legislation.

Mr. UDALL. Thank you for your testimony.

Chairman THUNE. Thank you, Mr. Udall. Mr. Shuster.

Mr. SHUSTER. Thank you, Mr. Chairman. As the Chairman said, I am from Pennsylvania. Most people who think of Pennsylvania, they think of Pittsburgh and Philadelphia. Well, I am from the center of the State, which is very rural, and I have over 7,000 farmers in my district, most of them small; so I have a keen interest in these two pieces of legislation because I think they assist and encourage small farmers to go out into the marketplace and be able to be more profitable.

And I want to thank all the panelists here today for their testimony. We have talked about a couple of these ventures. How many of them are out there? I know in Pennsylvania, I am familiar with the dairy co-ops, but for the most part they deal with shipping and distributing the milk, not taking it to the end user. So how many of these ventures are out there? Are there many or few? I don't have a sense of that.

Mr. REIS. I don't have a real sense of it either, but the USDA program that I told you we got a $500,000 grant for had 210 applications for that $10 million, and a very, very short application period. They gave us like 30 days to put this together. So I am sure there are a lot more of them out there that didn't apply.

Mr. SHUSTER. Go ahead.

Mr. NELSON. Regionally, there has been a lot happening over the last 10 years. Like North Dakota has been one of the leading States in developing these sorts of enterprises. I think they probably have, for sure, the most per capita, and probably have 30 or 40 different enterprises in the State of North Dakota with only 650,000 people. So that is really significant.

In South Dakota we are gaining, and in Minnesota. In Minnesota, for instance, there are 14 ethanol plants and 12 of them are operated by farmer-owned entities. So I would say nationwide there are getting to be quite a few.

Mr. SHUSTER. Where would I go to find out what is happening in Pennsylvania? The Farm Bureau, would they be the best source for me? Would they be tuned into this type of thing?

Mr. NELSON. They could be, but through the USDA and the Economic Research Service, in fact, if you go on the Web, you could find out very quickly how many value-added operations would be in Pennsylvania by going to their Web site.

Mr. SHUSTER. In South Dakota, how successful have these—you said about 30 or 40 ventures. How successful are they, on balance?

Mr. NELSON. In North Dakota. In South Dakota, ours have been very successful. We haven't done as much as they have in North Dakota and in Minnesota, but we are hopeful to catch up with them very soon. But we have been cautious in developing programs, and so far we have been fairly fortunate in having operations that have been very successful.

The fact that these are high risk has to always be at the forefront. There is no question that there is some risk involved, and because there is this risk, there are going to be some failures; but that shouldn't be reason not to do it, just because there have been failures in the past or will be some in the future. It is very important, we think, to move forward with these operations. If everyone was successful, then we probably aren't going fast enough or far enough.

Ms. JORDE. First of all, I was born in Bellfont, Pennsylvania; but commenting on North Dakota, like you said, there have been a number of them. Not all of them have been successful. I would say, though, when they say only one out of every ten new business start-ups makes it ultimately, I think the batting average is much higher for value-added cooperatives. There is a real commitment of leadership and a real drive to succeed. The farmers are very much driven to make this thing work, so they put in a tremendous amount of not only financial resources, but time, into the boards in developing the plan and attending meetings and getting out there and talking to farmers. So the motivation is tremendous.

Mr. SHUSTER. You said, Mr. Reis, there were 210 people that applied. Do you find that across the board in the other States that these——

Mr. REIS. That was nationwide.

Mr. SHUSTER. What, are you talking about the application——

Mr. REIS. For the USDA grant. I think a lot of them applied for the full 500,000, so you are talking $50-some million was applied for and only 10 was funded.

Mr. SHUSTER. And 210 nationwide doesn't seem to me to be a large number. Are there interests in the farming community nationwide? Again, 210 doesn't seem like a whole lot of farmers.

Mr. REIS. That is not farmers. That is co-ops.

Mr. SHUSTER. So it could be thousands.

Mr. REIS. It could be thousands. And if you look at Illinois, our co-op represents the whole State. That is one pork-producing plant in the State, and a couple of ethanols. Wheat is not as big a commodity as it is out West, but if you get 500 or 750, that is a lot of cooperatives.

Mr. SHUSTER. Are these ventures, are they—I know you talked about your hog-processing plant. That is from the barnyard to the shelf. Are most of them doing that kind of vertical integration, or are they just a portion of the integration?

Ms. JORDE. Well, I think our experience has been that, you know, whether it is sugar beets that come out of the field and go directly into the crystal bag sugar packages out the front door, or pasta that comes in the back door as durum wheat—it is milled in semolina and processed into all kinds of, you know, lasagnas and raviolis and everything else out the front door—we have seen total vertical integration.

Mr. REIS. Some of them take it a step further and make processed pizza dough. There is one in Oklahoma that just got started, and we are looking at the leasing company that leased their equipment to them. But they are taking the wheat from the farm all the way to the pizza dough, so all you have got to do is throw it in the oven.

Mr. SHUSTER. Are those cases limited where you are going to go from cradle to grave, so to speak? It seems to me that would make sense in the dairy industry. The dairy farmers aren't getting the profits in the store when the consumer buys it, so——

Mr. NELSON. The market is changing so much in the case of dairy. What used to be a throwaway byproduct, now in a powdered form used as a food additive, and other food additives as well, are actually worth more than the fluid milk in some cases. So it is a growth process, I think, of finding new ways, like Jay said in beef and Dave with pork, finding new ways to prepare it and market it.

I think in some of the existing value-added enterprises like the soybean plant in South Dakota, right now they aren't processing soybean oil to go right on the shelf, but they are looking at adding certain identity preserve-types of soybeans that could be used for the Japanese market or for some other European market, that then they would be able to do the processing and have that special product for the end user. But first they start out as kind of a bulk processing facility and then they will grow into that as time goes on. So some started out but are getting into it over a period of a few years.

Ms. JORDE. But I think the point we have to remember, and really the point of the hearing also, is that investing in value-added cooperatives is risky and it can take, many times, a number of years before the farmer really starts to get a return on his investment. And one farmer might have an investment in two or three or four different cooperatives, maybe smaller amounts. One or two of those may not work either, so they end up losing all their investments.

So we have really been asking our farmers to put up all the seed money and take all the risk in order to help rural development in our communities, and obviously their goal is that they want to be able to share in some of the profit from producing the product into the finished product. But it is still very risky, and farmers are tapped out, and they don't have risk money left. They are the ones that have been providing the equity capital to these projects, and there isn't a lot left.

Mr. SHUSTER. Mr. Reis, your hog venture, did you say 240 farmers?

Mr. REIS. That's how I——

Mr. SHUSTER. What was the average investment?

Mr. REIS. We sell on shackle spaces, which allows a producer to have one animal per week killed. That is how we set up the shares. Anywhere from 20 to 75 to 80 is the average purchase amount of shares. If they sell one semi-load a week, that is 180 shackles, and if they sell two loads a week, you know, you are getting up there to 360.

Mr. SHUSTER. What is the cost of a shackle?

Mr. REIS. We are going through the financing right now, but anywhere from $500 to $1,000.

Mr. SHUSTER. You are not in operation at this point?

Mr. REIS. No.

Mr. SHUSTER. One final question to Mr. Truitt. What markets are important to the beef industry internationally; or the most important, I should say?

Mr. TRUITT. Obviously, we would like to make sure that the Asian market continues to be recovering. I guess it has long been our number one and most important high-dollar or high-end export market. Mexico and Canada. Mexico specifically is a very important market for the United States as well, though. Japan is number one. But when we look into some of the products that we really don't use at all in this country or that fit easier into someone else's marketplace, Mexico is an important place for us.

The European Union as a market still has promise, but they have forgotten to keep all the agreements that the WTO required; so until we get that worked out that continues to be a tough spot for us.

Mr. SHUSTER. Have we been able to sell any into China? I am not familiar with what——

Mr. TRUITT. No, sir. Really, we have just begun to do some development in the marketplace there, but China obviously is a beef-deficit country from its own production standards. So we see it as one of those places over the horizon that we would like to be—I would say in response to your earlier question about the investments, I mean my investments range from $55 to $75 per head, so some of them are pretty modest into those cooperative agreements. And all of those investments have been returned back to me now, so I feel pretty good about them. I am glad to not be on the other end of that scenario.

Mr. SHUSTER. All right. Thank you very much.

Chairman THUNE. Thank you, Mr. Shuster. We have some folks in the room today from my State of South Dakota where cooperatives have been very successful; rural electric cooperatives in the room today. And that model is one that I think that makes a lot of sense when it comes to value added.

And you all have referenced the fact that there is a shortage of capital and equity and everything else, which is something that the tax credit bill that I introduced would attempt to at least provide some incentives for people. If it is a question of sending your money to Uncle Sam or putting it into something that might actually get you a return, I think that would be fairly straightforward for most farmers.

The good news, and there is a hearing going on right now in the Ag Committee—which I hope to make it over to—about the new farm bill. And in that new farm bill there is over the next 10 years $370 million set aside for value-added type opportunities, and I am hoping before it is all said and done to get a portion of that carved out for my bill, House bill 1093 that creates the Ag Innovation Centers. And really a lot of things you have talked about today, that you have testified to, are technical barriers as well, and these are complex things.

And Wayne, you had mentioned, and I think this is really true, that if we are not experiencing a certain number of failures, we are probably not being aggressive enough, because I think we are going to have to assume a certain amount of risk and accept a certain amount of failure when it comes to these types of ventures. But we cannot afford not to be investing; we just have to for the future of the rural economy.

Just a couple of questions and then we will wrap up pretty quick. Mr. Nelson, you had commented that your company, Communicating for Agriculture and the Self-Employed, it would seem to me to tie into sort of this question; and that is, how do we do a better job of getting the message out and educating people about the benefits and value of value-added agriculture? We have, I think, this mentality that is over a period of time in production agriculture, but how do we get more people in the country to buy into the whole importance of investing in these types of activities?

Mr. NELSON. Well, I think the first thing we have to do is to convince ourselves, convince farmers, and sometimes, you know, it seems like it should be a slam dunk, but it isn't always all that easy—as Dave, I am sure, will say in trying to get his project off the ground. There is a feeling that maybe farmers don't have enough confidence in their own ability, I guess would be the best way to say it. And I think that as David has proven, and countless other operations that have started and are successful have proven, that farmers do have the ability to get together with the proper guidance to do these projects. But there is a little bit of mistrust from the farm communities and from people in the rural communities thinking that are you really able to do this?

So I think, first of all, proving that you are able is the place to start. And the second thing is just to have a public hearing like this and do as much as possible to show that the results of this value added can be very, very important not only to the farmers themselves, which, of course, is of utmost importance, but also to these rural communities. And I don't think the impact on rural communities has been stressed enough. And I think that if we continue to say, look, this can be of help to Cando, North Dakota or to Murdo, South Dakota, to all of these smaller communities, they could be helped by value-added enterprises, and I think that is what we strive to do.

Chairman THUNE. I just think from the standpoint of economic development in rural areas, technology is a part of that, and I think, as was referenced, investment in broadband so that we have access to high-speed Internet service out in those areas of the country is really important, too. But if you look at what we have and do well, it is production agriculture. It is always going to be the number one industry in South Dakota, at least in the foreseeable future. So how can we take that and build upon it and make it something that can be profitable for producers? I think that is the big question.

Ms. Jorde, I think the story that you talk about up there is a fascinating one, and I love a town with a name of Cando. Incidentally, where did that come from?

Ms. JORDE. Well, my understanding is that there was a contest back when the town was named and the slogan "You can do better in Cando" was the winner.

Chairman THUNE. And you have done, I guess, when it comes to the pastaplant there. But walk us through, and obviously we don't have a lot of time to do this, but sort of the loan and financing process that your bank did in making that operation go.

Ms. JORDE. Well, this was over 20 years ago, in 1978, and at that time and still to this day, that particular plant is still privately owned by an individual that came out of the Twin Cities. His wife was from Bisbee, North Dakota, which is about 15 miles from Cando, and the owner had the dream of building the first pasta plant where the raw product, durum came in through the back door, was milled, into semolina, processed into pasta and shipped out the front door in his own brand name called Noodles by Leonardo. We worked with the owner, the two local community banks in the community, along with the Bank of North Dakota, which is our State-owned bank, somewhat similar to a bankers bank but actually the only State-owned bank in the country, and we put together a financing package along with a CDBG grant. And we were able to build the plant, and it has been operating now since 1978. And I really think from that plant, that was where some of the ideas started to continue the success that that plant realized, and farmers decided at that point that they could be involved with it, too. So other pasta plants in the area were built, and we have had great success in those areas, too.

Since then, the Federal and State and local programs have changed, but we have always found that there is never just one loan program or that just one bank can finance it. It has normally taken five or six or seven or eight different programs to bring a project to fruition, and that is why it is so important to bring in different players. And like you said, our electric cooperative in our community is a very important part of the financial packages that we put together, because of access that they have to some of the programs. So we try to work with as many local experts as we can.

Chairman THUNE. With farm income declining, have you seen like a drop-off in application rates for loans? How has that impacted your——

Ms. JORDE. Well, as far as individual loans, we still have farmers that need financing, in fact, more than ever. But we have fewer farmers. With our county losing 21 percent of its population in the last 10 years, obviously it is because we have had a loss of farmers and they have left the county in search of jobs in other areas. So our loan growth in the agricultural area has not increased substantially.

I think that the farm loans that we have on the books now are stronger than they have been in the past; but, you know, again, a lot of that is because of the government programs and disaster programs that have helped keep the farmers afloat. But there is no vision right now for the future, other than in value-added agriculture, and that is what has been so disappointing and disillusioning to a lot of farmers. That is why we don't have new farmers coming into the area, because they can't predict success very far into the future.

Chairman THUNE. Well, there is a quality of life in rural areas that is worth fighting to preserve, and I just happen to think that we have got to be at this level, the State level, the local level, private industry, working together as much as we can with this type of solution.

Obviously, as I said earlier, I have got some grave concerns about what we are seeing in terms of concentration in the agricultural marketplace and what that means to competitive markets and everything else, but until that changes, we really have to do what we can to take control of our own destiny.

So I appreciate your testimony. There are a number of barriers which you have indicated that we are aware of: capital, equity, the technical barriers some of you have alluded to. What we want to do is tear those barriers down as much as we can and provide incentives for our producers to form cooperatives to invest in these types of operations for their future.

So, Mr. Shuster, any other questions or comments?

I would welcome, as we continue in this dialogue and debate and discussion, your input as to things that we can do better. You are all out there in the real world dealing with these issues on a daily basis, and I am just very committed and dedicated to the whole notion of value-added agriculture and the difference that it can make in trying to at least preserve and save our rural economies. I think the family farming structure and everything that is associated with it is so important, not only from an economic standpoint but also from a social and cultural standpoint and what it means to this country and its future. So we definitely need to be coming up with ways and solutions that make sense and that will further the cause, I believe, of value-added agriculture in America.

So thank you all for your testimony. It has been very helpful, and, as I said earlier, we welcome your ongoing input in this process. With that, this hearing is adjourned.

[Whereupon, at 11:44 a.m., the Subcommittee was adjourned.]

JOHN THUNE, SOUTH DAKOTA
CHAIRMAN

TOM UDALL, NEW MEXICO
RANKING MINORITY MEMBER

Congress of the United States
House of Representatives
107th Congress
Committee on Small Business
Subcommittee on Rural Enterprises, Agriculture and Technology
2361 Rayburn House Office Building
Washington, DC 20515-6319

Opening Statement

Chairman John R. Thune

"Regrowing Rural America Through Value-Added Agriculture"

**Subcommittee on Rural Enterprises,
Agriculture and Technology
House Committee on Small Business
July 17, 2001**

Good morning.

Today's hearing has been called to discuss how we can regrow rural America through value-added agriculture. Agriculture is the life-blood of many rural state's economies, and value-added enterprises will greatly aid the revitalization of rural communities.

Producers want and need to reach up the agriculture marketing chain and capture the profits generated from processing their raw commodities in order to compete in an increasingly concentrated marketplace.

The family farmer is America's original small business owner, and in today's concentrated ag marketplace, producers have often been forced to accept lower prices for their commodities.

This trend towards consolidation has been very pronounced during the last decade. For example, the hog industry has consolidated rapidly, with the four largest firm's share of hog slaughter now reaching roughly 57%, compared with 32% in 1980.
In the cattle sector, the four largest beef packer's account for about 79% of all cattle slaughtered, compared with 36% in 1980.

In addition, from 1984 to 1998, consumer food prices increased 3% while the prices paid to farmers for their

products plunged 36%. The average wheat farmer, for instance, earns about 3 cents on every box of Wheaties and about 5 cents on a loaf of bread.

The problem facing Congress is how to help farmers become "Price Makers" instead of "Price Takers." To many of us, expanded opportunities for value-added enterprises are the answer.

While producers have great interest in pulling together to add value to their products, two primary barriers stand in the way. First, producers do not have the technical expertise to launch extremely complex business ventures, like value-added cooperatives. Farmers are outside their arena when it comes to putting together processing plants. Second, producers are currently cash strapped. Even if enough investment capital could be accumulated to initiate development of producer owned value-added processing, many of the consolidated players in the market could squeeze producer owned entities out before becoming profitable.

To help jump-start the process, I, along with my colleagues Jo Ann Emerson of Missouri and Dennis Rehberg of Montana, have introduced two bills to assist farmers who want to create new value-added enterprises.

H.R. 1093, The Value-Added Development Act for American Agriculture, provides $50 million in grant money to states to form agriculture innovation centers. The Ag Innovation Centers would provide desperately needed technical expertise – engineering, business, research, and legal services – to assist producers in forming producer owned value-added endeavors.

H.R. 1094, The Value-Added Agriculture Investment Tax Credit Act, allows producers to receive a 50% tax credit on investments in producer-owned value-added enterprises. The bill provides a maximum tax credit benefit of up to $30,000 per year per producer, and the tax credits may be applied over 20 years.

Congress needs to help provide opportunities for producers to create new value-added ventures, and these two bills are an inexpensive way to accomplish that goal.

I want to again thank the witnesses for appearing before our subcommittee today, and we look forward to hearing your testimony.

Statement of Congressman Tom Udall
Ranking Member, Subcommittee on Rural Enterprises,
Technology and Agriculture
"Regrowing Rural American through Value-Added Agriculture"

Tuesday, July, 2001

Thank you, Chairman Thune:

The importance of value added agriculture continues to grow every year. It grows in part because farmers and agricultural producers want a more profitable and efficient operation. As the economics of farming continues to change, value-added agriculture and production will allow farmers to better control their future.

Everyday farmers and agricultural producers are exposed to both production and price risks. Production levels can vary significantly from year to year based on weather or natural disasters. Moreover, production levels and demand conditions, both domestically and internationally control the prices farmers receive for their commodities. States and communities, alike, are looking to broaden their economic base using agriculture as their foundation.

In my Congressional District, communities, working with the New Mexico Department of Agriculture are taking charge of their destiny by adding value to the way they do business. For example:

- Sheep production has been an integral part of New Mexico agriculture since the first Spanish settlers arrived to the southwest. Sheep have been the animal of choice because of their ability to survive and produce food and fiber in the relatively harsh environment of the region.

However, the situation has become critical for the survival of the sheep industry and sheep dependent families in my state. Low prices for lamb and wool, coupled with increasing imports have taken a toll on the industry. The New Mexico sheep flock has declined dramatically, from 730 thousand in 1970 to about 280 thousand sheep in 1999.

New Mexico sheep producers are presently producing 2.3 million pounds of wool. If these producers are forced to rely on traditional regional wool outlets, they will only receive a depressed market price.

One way to help alleviate the increased pressure on sheep and wool producers in New Mexico is to add value to the wool through dying the predominantly white Merino wool into high quality yarn that could be marketed in the immediate region.

Currently, the wool producers are working to determine the regional market for high quality wool fiber products and are generating a financial base for future product and market development.

Another example deals with Organic Wheat Production:

- Currently, growers in Costilla, New Mexico have established a flour mill that will produce whole wheat and white flour enabling them to capture the value-added component of their wheat. Using this flour mill will more than double their returns, in addition to creating three or four jobs in a high unemployment area of New Mexico. The growers previously sent their wheat to Colorado for processing. The mill will help to create a complete line of value-added products based upon organic wheat produced in the region.

These are just two examples of value-added ventures that are taking place in my district and throughout my state. Unfortunately, New Mexico, is one of about a dozen states, that do not subsidize loans or offer loan guarantee programs, grants, tax abatements, or other financial incentives to businesses that process agricultural products. In my state, the New Mexico Department of Agriculture assists farmers and agricultural producers in locating funding from private entities as well as providing demonstration project money where they can.

It is my hope that this hearing will provide a forum in which we can find ways to help create a more productive environment for the creation of value-added ventures. I would also like to inform you Mr. Chairman, that I have recently co-sponsored H.R. 1093 and H.R. 1094 which you along with Representatives Emerson and Rehberg have introduced to help producers capture more value from their products through producer owned value-added processing.

Thank you Mr. Chairman.

Testimony of Wayne Nelson, President
Communicating for Agriculture & the Self-Employed

Before the U.S. House of Representatives
Small Business Subcommittee on
Rural Enterprises, Agriculture and Technology

Hearing on
"Regrowing Rural America Through Value-Added Agriculture"

Tuesday, July 17, 2001
Washington, D.C.

Chairman Thune, members of the Committee, I thank you for the opportunity to speak to you today about a issue that has long been a priority to the members of our organization…an issue that we believe is a vital part of long-term strategies for the success of Rural America – **how to spark the development of successful value-added agricultural enterprises.**

My name is Wayne Nelson and I serve as President of Communicating for Agriculture & the Self-Employed (CA). I also have been a grain farmer in western South Dakota for 30 years. CA is a national, non-profit rural organization made up of farmers, ranchers and rural small business members from across the nation. CA was founded in 1972 in Fergus Falls, Minnesota and continues to be headquartered there. CA works on a variety of legislative and public policy issues, and also provides a range of benefit programs and information services for our members, including operating what has grown to be the largest international agricultural exchange program in the U.S But among the purposes of our organization, none is more important than our goal of keeping rural America alive and healthy in terms of our individual farmers and our rural communities.

Mr. Chairman, we want to thank you for calling this important hearing to discuss ways to enable value-added agriculture to help farmers and build new jobs and a stronger economic base for rural communities. Value-added agriculture is not a panacea to instantly bring us out of our continuing slump of low commodity prices, especially in grain. But it certainly is an important tool to put in the toolbox of efforts we need to have to create a thriving rural economy.

To summarize the points I would like to make today:

- I want to point out some of the **reasons why value-added agriculture development is so important** – a vital part of long-term strategies for farmers in our rapidly changing food and agricultural system. We must get more serious about getting the job done than we have been in the past.
- We want to convey **CA's support for certain legislation and programs – specifically H.R. 1094, the "Farmers' Value-Added Agricultural Investment Tax Credit Act"**; and for H.R. 1093, and other technical assistance programs in value-added agriculture development; and for strengthening existing programs like USDA's Value-Added Co-op Stock Purchase Loan Guarantee program.
- And, I'd like to reiterate CA's support for other legislative measures that we think are also **important additional tools for the family agriculture policy tool box** – including legislation that would strengthen anti-trust oversight to preserve competition; legislation that expand beginning farmers finance programs; and several constructive tax proposals contained in H.R. 2347 and S. 312, commonly known as the Ag Tax Package.

There are many reasons why value-added agriculture development is important, but the most fundamental reason is simply --- low farm income. This is the fourth consecutive year of drastically low farm prices. Today we are preparing to harvest wheat on my farm and the price is over one dollar less than the cost of production. The markets have been consistently low for all the major crops. Livestock and dairy prices have swung widely, but the damage of the low price periods has outweighed recent periods of recovery.

This underscores the critical importance of federal farm program dollars to supplement farm income. It also underscores the need for new, additional sources of farm income.

A second key reason to strengthen value-added agriculture has to do with the fundamental changes underway in the structure of the farm economy. **It is now abundantly clear that vertical integration in agriculture is here to stay.**

Today, reports say that only 17 percent of hogs are sold on the open market. As recently as 1997 that figure was 43 percent. The change of the hog market from open market to contract and other vertically aligned or owned production has come very rapidly. We feel this momentum indicates it this vertical integration will soon be a reality in all sectors of agriculture, including the grain markets.

This is a cause of great worry among farmers, but the results of this trend are by no means necessarily bad. **Vertical integration can have many benefits – the only question is, will farmers truly participate and will they share in its rewards?** Or will they simply be the lowest end vendors who get little reward but shoulder the lion's share of the risk.

Vertical integration from the farmer's field to the grocery shelf offers the opportunity to better line up supply with demand. It also offers the opportunity to produce more specialized, tailored products that consumers want, whether it's lean pork, organic vegetables, branded beef products, or specialty grains. It offers the opportunity to produce better products for our customers. That kind of change is progress, it's good.

Both of these opportunities, if the new system is working right, should result in additional income for the farmers in this kind of system. After all, it often takes additional investment and more labor and management to produce these more specialized products.

But the fact is, the result of more farm income is not a given. An example of how the vertical integration trend has not delivered more reliable, improved farm income is, again, in the new hog market. Many of the hog marketing contracts base their price on the open market, which has a rapidly decreasing percentage of marketed hogs determining the price. That open market, which is made up of only 17 percent of all hogs marketed, accounts for the pricing of 71 percent of market hogs – so only 17 of the 71 percent represents a negotiated price, according to the University of Minnesota Extension Service. The point is, it is highly questionable if the market price accurately reflects true supply and demand, and even more questionable if farmers are being paid a better price for producing a better product under this system.

Value-added agricultural enterprises will work best; deliver their promise, if the farmers share in the benefits and rewards as well as the risks.

In this new farm economy, the old tools we've used to try to shore up and protect farm income simply aren't enough to do the job. We need a bigger toolbox, and some new tools.

1. Certainly the new farm bill Congress is about to write will be extremely important. CA believes it is vital that we continue to have farm income support programs, and share the views of many other ag groups that they should be counter cyclical, and factor in incentives and payments for stronger conservation. The last four years makes it clear that farm programs have been, and will continue to play a vital role in providing a safety net for farmers.

2. However, in this new vertically integrated farm economy, CA sees a need for new policies and programs involving education, oversight and regulation of contracting. If the majority of farm commodities are going to be produced under contracts, it stands to reason policy makers need to look at ways to prevent abuses and unfair discrimination in the use of contracts to preserve the rights of family farmers, and preserve access to markets. CA also sees a need for stronger federal anti-trust oversight and effort to preserve competition in agricultural markets and supply chains. Farmers are greatly concerned about the growing concentration in the agricultural industry. The rate of mergers and takeovers in recent years has been unprecedented. We're seeing companies move to clearly dominate certain markets.

We commend the Chairman for introducing H.R. 1526, the Agriculture Competition Enhancement Act , which would put limits on mergers to prevent excessive concentration, and provide for stronger oversight in the Department of Justice by establishing an Office of Special Counsel for Agriculture. CA is encouraged by the interest in reining in concentration shown by members of both parties in the Senate and House, and we urge Congress to put together strong, consensus legislation that will strengthen both USDA's and the Department of Justice's hands in preserving competition. The recent mandatory livestock price reporting program by USDA demonstrates it is not easy to put these systems in place in this new farm economy, but it shows it's necessary, and we believe just a start in preserving fair market access.

3. CA believes one of the best ways to address vertical integration is to find ways for farmers to participate as equity holders of value-added enterprises, both cooperatives and through various joint ventures.

Whereas anti-trust enforcement, contract rules and full market reporting represent defensive tools for preserving family agriculture, value-added agriculture represents a constructive tool to build a better agricultural system. We recognize that the enormous productive capability of the American farmer in producing bulk commodities still points to the need for a continued strong export policy; but value-added agriculture can go a long way toward increasing farm income and adding benefit to rural communities.

We don't want to the landscape of rural America to look like a few giant farms and a few giant corporate processing facilities located hundreds of miles away in large cities. We like the present mix of family farms and would like to see processing facilities located in rural communities providing more jobs and income. We recognize that change is inevitable, and the best way for farmers to address this change is to participate directly as partners.

There is opportunity in value-added agriculture. In my home state of South Dakota farmers are operating their own new soybean processing facility that has created a better market and price for their product. In CA's home state of Minnesota, 12 of the state's 14 ethanol plants are cooperatives owned by their farmer suppliers. They are looking to expand their plants, and there are new cooperatives plants being considered in states across the Upper Midwest and other parts of the country.

Among new and better tools we think would help:

* CA offers our support and encouragement that Congress approve H.R. 1094, the "Farmers' Value-Added Agricultural Investment Tax Credit Act". As you know, this bill calls for allowing

producers to receive a 50 percent tax credit on investments in producer-owned, value-added enterprises. The tax credit could be for up to $30,000 per year, and applied for over 20 years.

This is a very significant incentive to assist in the development of new co-ops and other value-added ventures, and we believe this kind of investment assistance is needed. People from USDA and others involved in rural development tell us there is very high interest by producers in these new cooperatives, but that it is very difficult now to find equity capital to get them going. Four years of low farm prices has really sapped the investment ability of many producers. While this legislation won't eliminate the risk inherent in these new ventures, it would give meaningful help to farmers' ability to participate in these businesses.

* H.R. 1093, a companion bill to the value-added investment tax bill, calls for USDA to administer grants that would go for establishing innovation centers to provide technical assistance, market and business development services for new value-added ventures. We think this is a worthwhile proposal, and we believe we need continued support and resources for existing cooperative assistance programs now in place.

As everyone knows, starting a new business is a very time-consuming, risky business. Farmers must take leadership and put their own time and money on the line for these to be successful. But the reality is, producers also have limits on how much time they can devote to these start-up efforts while continuing to meet the work demands of their farms. There is a need for knowledgeable, hands-on technical assistance to not just evaluate new value-added ventures, but to do the business planning and organizing to make them better proposals with a greater chance for success.

* USDA's Cooperative Stock Purchase Program, offered through the Rural Business-Cooperative Service enables farmers to use B&I loan guarantees to help pay for stock in a start-up, value-added cooperative. CA believes the program needs continued funding, and we need to look for ways to improve this and other cooperative assistance programs in USDA.

* CA also believes it's very important for us to find ways to help new, beginning farmers to participate in value-added agricultural enterprises.

CA has a long history of working to establish and enhance beginning farmers and ranchers programs. We believe if we are going to preserve family agriculture, one of the most fundamental priorities is to provide support to our next generation of farmers and ranchers. If the new farm economy is going to consist of vertically integrated systems, hopefully with strong, direct farmer ownership and participation -- then we must see that beginning farmers have the opportunity to also participate, not only the better financed, established producers.

Toward that end, we'd recommend that Congress and USDA establish a new direct loan program that would provide lower interest rate financing for qualified beginning farmers to participate in value-added cooperatives.

I'd like to touch on a few other current legislative proposals that CA believes are important, and would contribute to building a stronger, sustainable family agricultural system.

Communicating for Agriculture, working in conjunction with the National Council of State Agricultural Finance Programs, is recommending two key proposals that would greatly enhance and help expand state and federal beginning farmers programs.

* Approve legislation that would exempt state "Aggie Bond" beginning farmers programs, which coordinate the use of federal tax-exempt private activity bonds to finance beginning farmers, from state bond caps. This proposal is included in H.R. 2347, the Tax Empowerment and Relief for Farmers and Fishermen Act, introduced by Rep. Nussle, that's known as the TERFF or Ag Tax Package. And it's in the bipartisan Senate companion overall ag tax bill, and as a stand alone bill. These small beginning farmers loans are quite different from the much larger housing and manufacturing project uses of tax-exempt bonds, yet they must compete with them for bond allocation by the states. This is preventing these very useful, cost efficient programs from serving the number of beginning farmers who apply in some states, and it is limiting our ability to get other states to start their own Aggie Bond programs.

* Approve legislation that would allow the Farm Service Agency beginning farmer loan guarantees to be used on Aggie Bond loans. They are the same type of loan. By combining these two programs, the lenders will be more willing to provide loans to beginning farmers, and eligible beginning farmers get the benefit of the lower interest rate through the Aggie Bond loan. These are existing, long proven, public/private programs that have demonstrated their service to beginning farmers. And these would be two, relatively simple, tax policy changes in the operating regulations that would do a great deal to expand the use of these programs.

* And on behalf of CA, I would like to express our support, and urge members of this committee to support, passage of the entire Ag Tax Package, H.R. 2347. The TERFF bill includes a range of important tax changes and programs that would benefit agriculture. Among them are FFARRM Accounts, which would provide for tax-deferred savings accounts to enable farmers and ranchers to save in good years for use in bad years; needed clarification of IRS rules regarding taxation of income from CRP payments and certain farm rental payments; the beginning farmer bond program state volume cap exemption; and others.

Also included in H.R. 2347 are some specific proposals that would benefit certain value-added agriculture enterprises -- including rule changes enabling cooperative marketing to include value-added processing through livestock; the small ethanol producers credit; the alcohol fuel credit; and rules regarding payment of dividends on stock of cooperatives without reducing patronage dividends.

In summary, CA believes we need new, additional tools in the agricultural policy toolbox to put our family agricultural system back on sound footing. Value-added agriculture is not a panacea, but it is one of the more important strategies that we need to pursue more seriously than we have in the past.

We have all talked a good story about value-added agriculture and the need for farmer participation for many years now. But the truth is, it is not an easy goal to achieve. The new ventures are risky. We have seen numerous success stories, but there have been failures too. Farmer need assistance in two critical areas for value added agriculture to succeed – help in financing their investment in these ventures, and competent, impartial technical assistance that can help develop worthwhile projects.

HR. 1094 is the most significant investment assistance proposal to come along and represents the level of support that is needed, and we urge that it be approved.

Thank you.

Statement of Terry Jorde – ICBA
Small Business Committee
July 17, 2001

Review of Value-Added Agriculture

Thank you Chairman Thune and other members of this subcommittee for holding today's important hearing on value-added agriculture. I applaud you for the work you have done on this issue. Your focus on value-added agriculture is much needed and timely given the current difficulties facing farmers and our rural communities. ICBA will continue to work with members of Congress and others on ways to increase investments into rural America and provide for new economic opportunities for our nation's farmers and ranchers and our Main Street businesses.

My name is Terry Jorde, and I serve on ICBA's Agriculture-Rural America Committee. I'm also the President and CEO of CountryBank USA, an agricultural bank located in the small community of Cando, which is in Towner County, North Dakota. CountryBank USA is a $35 million asset bank and most of our loans are agricultural credits. In addition, my family owns a potato and grain farm. Our town has 1,300 people and is heavily dependent on the agricultural economy.

ICBA is the only national trade association that exclusively represents the interests of our nation's community banks. Over two-thirds of ICBA's member banks are located in small communities of under 10,000 population. Over three-fourths of our membership serves communities of under 20,000 people. Eighty-six percent are in communities of less than 50,000 population. Clearly the ICBA as an association and its' community bank members across the nation have a long standing interest in ensuring credit availability to our nation's farmers, small businessmen and women and other consumers in our nation's rural communities. We also have a strong interest in rural development initiatives that can underpin a strengthened farm safety net and help diversify our rural communities.

Adapting to a Changing Economy

In our small community we have worked very hard to create new jobs over the past decade. New residents and displaced farmers have been attracted to the jobs in a pasta plant and a foundry. They have also been employed at construction sites, a medical center and a health and dental clinic. Our bank has served primarily an agricultural base for many years. However, we have tried to diversify our asset base and revenue sources. We continue to work with our farm customers on developing long-term business and investment strategies for the 21st Century global economy that we now participate in.

All of us know all too well about the difficult times facing America's farmers – times made less difficult by massive infusions of government financial aid the past couple of years. Despite this welcomed financial aid, many farmers have been left to wonder just how long these fundamental problems will last.

Many farmers have had to turn to off farm jobs to keep their farms afloat. That is why diversifying the economic base of our rural communities is so important and why rural development, which encompasses value added agriculture, is such a crucial issue. The need for stronger rural economies is also why our approach to sustaining rural America needs to go beyond the traditional realm of crop supports -- as important as they are.

Helping a Community Prosper and Grow

CountryBank USA, like many community banks across the nation, has tried to be a catalyst for rural development in our small town of Cando. Cando established an economic development group called the Durum Triangle Development Corporation back in 1978. That organization has now evolved into a county-wide development corporation whose nine member board consists of two community bankers, an attorney, our hospital administrator, a city council member, a county commissioner, and other representatives of our county.

Our experience has shown that before investing in a new rural business project a farmer, banker, or any entrepreneur needs to ask a most fundamental question – "Can we do this – Does this make sense?" If it does, then we stress developing a written business plan or concept paper to figure out how to structure the debt-financing and how to attract equity capital, which is in short supply in many rural areas, for the project. We're pleased to have had some successes.

Our community bank participated in the first totally integrated pasta plant in the nation. About 20 years ago, very little durum wheat was milled in North Dakota. Now, well over 10 percent of all U.S.-produced durum, which is the best wheat for making pasta, is being milled there. In Cando and other North Dakota towns, durum comes in the back door of the plant, is milled into semolina, and is processed into pasta, which is packed and sent out the front of the plant to the consumers across the U.S. This has created 500 jobs in the local pasta industry.

Our bank has also participated in a loan to a local foundry that casts small agricultural implement parts. We became aware of a Canadian foundry owner who was considering a U.S. foundry because many companies want their products to carry the "Made in the USA" label. We showed them why they should locate an American plant in Cando. We brought lots of people together with various types of expertise – two bankers, an attorney, a state legislative representative and the president of the electric cooperative.

They opened for business in the fall of 1995, and now have about 90 employees. These types of loans allow small rural communities to grow and diversify their economic base, adding value to the local economy. Yet despite these efforts our county has lost nearly twenty-one percent of its population according to the last census numbers from 1990 to 2000. Clearly we have to do more.

Key Principals To Drive Rural Development Policies

We appreciate this hearing today Mr. Chairman because we believe that a strong rural economy must go beyond simply writing a new farm policy. Therefore, Mr. Chairman, I would like to suggest three basic principals that should underlie the federal government's approach to implementing a sound and broad-based set of rural development policy initiatives. These principals are:

1) Target Resources to Rural Communities based on population;
2) Provide Tools To Complement – Not Compete With -- the Private Sector;
3) Target Resources to Various Sizes of Businesses, Including Individuals; and
4) Maintain the Population Base and Infrastructure of Rural Communities;

Target Resources to Rural Communities -- We need to ensure that programs first and foremost truly target rural areas and lead to the creation of new jobs and to business start-ups and business expansions. This means there should be a population-based criteria as the first component of deciding where federal monies go, such as the Business and Industry (B&I) program's requirement that loans go to communities of 50,000 or less.

Limited flexibility to go outside of rural areas could exist when the benefits can be shown to directly help farmers. However, the flexibility for funding should be limited to the extent that such "non-rural" funding should never represent a majority of the rural development program's funding. Otherwise, we are talking about "Rural Enhancement" with only indirect benefits accruing to rural communities. We need to be sure to keep focused on job development within rural communities.

We need to be sure our rural development programs are well coordinated and work together and that rural citizens have adequate access to information about programs.

There are many benefits of targeting rural areas with the lion's share of rural development dollars. These include:

1) Providing off-farm jobs for farmers;
2) Maintaining the local tax base;
3) Maintaining the population base which is necessary to keep experienced local leadership and a skilled workforce in our rural communities; and
4) Maintaining the infrastructure and services available to our rural communities.

Recognize and Complement the Efforts of the Private Sector -- While an enhanced role for rural development policies is extremely important, ICBA believes a second fundamental principal of rural development policies is that they must be made to compliment and add to – not compete with and subtract from – the efforts of the private sector, especially private sector financial institutions. Many residents in rural communities will tell you that the community banker is the leading catalyst to bringing together the people and leveraging the resources necessary to attract new businesses to the rural community.

Congress must not diminish what the private sector is already doing or rural development efforts will be sparse and ineffective. This would include formulating any policies that allow the Farm Credit System, a government sponsored enterprise, or other new government assisted players into rural business lending to simply take away good business loans that the private sector is already making. So we stress that federal policies should only be complementary to what the private sector is already trying to do.

Specifically from the standpoint of community banks there should be a recognition that there are thousands of community banks in our rural areas that can help stimulate our rural economy if they are given the right tools. For example, there are approximately 3,000 "agricultural" banks alone and several thousand non-ag banks all in rural areas. Rural development policies need to be intricately tied into this vast network of private sector lenders if these policies are to be successful.

As stated at the outset of my testimony, over 75% of ICBA's 5,000 members are in towns of less than 20,000 people. 86% are in towns of less than 50,000. Congress should develop and expand existing tools that can be utilized by this vast network of private sector community banks. **One obvious way to do this is through greater use of guaranteed loan programs.** These banks are keenly aware that the future of their institutions are directly tied to the future of their rural communities.

Target Resources to Various Sizes of Businesses, Including Individuals – In an era of limited funding we need to make sure that scarce federal dollars are targeted to achieve the most impact possible in our rural communities. In addition to targeting rural communities based on population, we need to ensure that credit is available to individual entrepreneurs as well as larger corporate and cooperative ventures. Obviously it may be easier to get financed if you are a multi-million dollar business interest. But we need to also ensure that individual entrepreneurs can thrive in a rural environment.

For example, one of my customers is a farmer who started a business that uses flax straw to make erosion control logs that are shipped all over the country to minimize erosion after flooding or forest fires. He is further expanding his business to make hanging basket liners for horticulture use out of absorbent and environmentally friendly flax blankets. He bought a closed-up school for $1.00 for the manufacturing site and our bank has helped fund this value-added project with the help of an SBA 7(a) guaranteed loan.

Maintain the Population Base and Infrastructure of Rural Communities -- Helping rural communities diversify their sources of income and their local economies is important because more and more farm families appear to be relying on off-farm income to support the farming enterprise. USDA statistics indicate that a significant part of the total income of farm households comes from off-farm sources. These off-farm earnings are reported to have averaged approximately $60,000 last year, up considerably from an average of $36,000 in 1992.

Yet trends indicate that counties which have relied largely upon agriculture as the main industry lost significant population in the last decade. For example, the FDIC's first quarter 2000 Regional Outlook report on the Kansas City region highlighted these troubling trends. Only about one quarter of the 400 rural counties studied were growing.

The recent 2000 census revealed that while the general population grew 13 percent in the 1990's, 676 counties, primarily rural counties, lost population. Those counties losing population are largely dependent on agriculture. This shows the importance of diversifying our rural economies because doing so will help keep people in rural America and will help farm families have additional sources of income thereby reducing the need to rely solely on farm programs for survival in rural America. The more diversified economies in rural America appear to be the most viable for the long term.

Maintaining a stable population base in rural areas is important because many demographers say that at some point the populations of communities can fall below a critical mass, destining them for an irreversible decline because they lack the human resources needed to remain viable. The per capita cost of providing services becomes too expensive. Ultimately keeping people, leaders, workers, and citizens in rural communities is essential to keeping a healthy rural social infrastructure in place, which is the foundation of a diverse economic base in our rural communities.

Three-fourths of our nation's counties are rural, most of which have populations under 50,000. A quarter of these counties have populations under 10,000. Of the nearly 40,000 governmental units in the United States, two-thirds have populations under 2,500, and nearly half have populations of less than 1,000. The elected officials in these jurisdictions are mostly part-time public servants, with minimal staff and/or decision support resources.

Maintaining the social infrastructure in terms of human resources is key to maintaining a viable physical infrastructure-- adequate roads, schools, health care services, utilities, Main Street businesses and, yes, locally owned community banks focused on meeting local financial needs.

From the standpoint of the community banks in these rural areas, the loss of population, with its subsequent result of fewer depositors and fewer deposits, is a critical problem since fewer deposits mean fewer funds available to make loans to local businesses and citizens and therefore less investment in the physical and social infrastructure of rural communities.

Necessary Tool Box For Fixing Rural Development

Mr. Chairman, we would suggest that a combination of policy tools are necessary for addressing the needs of rural America. This "tool box" should include:

1) Appropriate tax incentives to spur new investment;
2) Enhancement of existing programs; and
3) Adoption of appropriate new programs.

Let me address each of these categories.

Appropriate Tax Incentives To Spur New Investment

HR 1093 and HR 1094 -- ICBA welcomes your legislative efforts to help producers capture more from their raw products through value-added processing. Value-added processing helps producers capture more of the food dollar higher up the marketing chain. HR 1093, the "Value Added Development Act for American Agriculture" provides for grants to assist value-added agricultural businesses. HR 1093 would grant $50 million to create Agricultural Innovation Centers for three years on a demonstration basis. These centers will provide much needed technical expertise to assist producers in forming their own value-added business. Assistance provided by these centers would include legal services, help with research, guidance with the engineering of the facility, and business advice.

This type of initiative could be very useful. For instance, last week USDA announced they were awarding a $5 million multi-state grant to establish the Agricultural Marketing Resource Center (AMRC), a dynamic collaboration of university research and outreach specialists focused on collecting and interpreting information and creating new research to support value-added agricultural activities. The universities involved in this effort would each have wide networks capable of directing resources, research and experience to value-added agriculture issues.

For example, North Dakota, known to be a leader in value-added cooperatives, has had a similar, but smaller program funded by the North Dakota legislature. It is called the Agricultural Products Utilization Commission. APUC provides grants for feasibility studies and start up technical expertise and has been a critical component for getting value-added projects off of the ground.

More of these types of multi-state initiatives should be pursued in an effort to provide additional resources for the development and marketing of value-added ventures. Again, I want to stress that given the thousands of community banks that exist in our rural areas, these efforts should be coordinated with bankers' involvement so bankers can help bring these resources and research to the attention of other leaders in the rural communities. We believe your legislation would help provide greater education and technical assistance to rural communities and bankers would stand ready to assist in these efforts.

Your legislation, HR 1094, the "Farmers' Value-Added Agricultural Investment Tax Credit Act", allows a tax credit for an investment by farmers in value-added businesses to create new economic opportunities for farmers. The bill provides incentives for farmers and ranchers to claim as much as a $30,000 credit for his $60,000 investment toward the purchase of producer-owned, value-added enterprises. Tax credits are helpful because farmers are limited in amounts they can invest, as are other rural businesses. We note also that the House Agriculture Committee's recently released farm bill draft contains a section that would provide grants for start-up farmer-owned value added processing facilities. We believe there is merit in such proposals, especially if they are targeted to rural communities, as we discuss earlier in our testimony.

Subchapter S Reform -- ICBA supports the Small Business and Financial Institutions Tax Relief Act of 2001 introduced in both the House and Senate (H.R.1263) and (S. 936). This legislation would help ease the tax burden on thousands of small businesses and community banks and free up capital to reinvest into the local communities they serve.

This legislation would afford many small businesses, including community banks, needed relief from punitive double taxation and would improve the viability of our nation's small banks and the communities they serve. When Congress passed the Small Business Job Protection Act of 1996, it made community banks eligible to elect S Corporation status for the first time in tax year 1997. Unfortunately, many community banks and small businesses are having trouble qualifying under the current rules and cannot benefit from Congress intended tax relief.

Subchapter S liberalization would correct many obstacles that often prevent small businesses and community banks from converting to Subchapter S. The key focus is on expanding the number of eligible shareholders for Subchapter S tax status from 75 to 150.

Promote Greater Use of Ethanol Legislation -- Mr. Chairman, I also want to applaud the efforts of you and other farm state congressmen and Senators in promoting greater use of ethanol. We seem to have two problems in this country where one could help solve the other. By this I mean that the surplus of ag commodities could be used to help meet the growing demand for energy in our country. Certainly this is value added agriculture since ethanol production adds 30 cents to the value of a bushel of corn and adds $4.5 billion to U.S. farm income annually. In addition it creates jobs in rural areas – 200,000 have already been created in rural America from ethanol production. In addition, ethanol has the potential to reduce our dependence on foreign oil imports and can contribute to the reduction of air pollution. One essential step among many would be for Congress to extend the federal ethanol tax incentive program as it considers comprehensive energy policy legislation this year.

Enhancing Existing Programs

Increase Deposit Insurance & Index it to Inflation -- Another key ingredient to providing more funds for investing in our rural communities would be to significantly increase deposit insurance and index it to inflation. Many rural banks are having difficulty growing their core deposit base which forces them to seek other, more expensive sources of funding to meet the lending needs of their rural communities.

While American agriculture is undergoing dramatic changes resulting in fewer and larger farms as well as larger corporate and agribusiness interests, deposit insurance hasn't been raised since 1980 and its value has been eroded in half, to approximately $50,000 based on 1980 dollars.

Increasing the deposit insurance level and indexing it to inflation would be a quick and efficient way to immediately help infuse more funds into our rural areas and ultimately benefit rural citizens, including farm families that depend on off-farm income to survive.

Increase funding for USDA's Business & Industry Guarantee Loan program -- We were pleased that Congress last year provided the USDA Business and Industry (B&I) program with a significant funding increase of 50 percent, bringing the budget to $1.5 billion for the current fiscal year. This program lends money to any rural business that provides economic opportunity to people living in towns with populations of less than 50,000 people, including gas stations, factories, and other local businesses. USDA reports that B&I loans reportedly saved or created more than 29,000 jobs last year. This is good news for banks in their efforts to help stimulate slow-growing rural markets. However, we are told that only about 400 banks are currently taking part in the program and more are trying to get in. The main problem has traditionally been that the B&I program is under-funded. Last year almost $1 billion in guaranteed loans, for nearly 400 projects, could not be approved due to lack of funding.

Given the statistics that show the loss of population in many agriculturally dependent counties and the need to diversify our rural economies to also strengthen our farm economy, we believe that providing more funds for the B&I program could be a very cost-efficient approach to strengthen the rural safety net and the farm economy. Remember that the lenders are the ones providing the funding, the government's expense comes only in cases of a loan default.

We would also suggest that the B&I program significantly target small businesses to ensure smaller rural projects receive the same consideration for funding as larger rural projects.

Limit/Eliminate Fees on Guaranteed Loan Programs in Rural Areas -- USDA's FY 2002 Budget included an increase in the loan origination fees on B&I guaranteed loans to 3.25 percent, well above the current 2% level. USDA apparently intends to implement this through a regulatory change since USDA believes a legislative change is not necessary. This increase to the guarantee fee will have an adverse impact on access to credit for many rural businesses as it will make the costs greater for the businesses. Many community banks will be unable to absorb these new, burdensome costs, especially at a time when agriculture and our rural economies are struggling.

The FY 2002 proposed budget for SBA suggested new fees on the SBA 7(a) loan program. Currently, both the borrowers and the lenders pay significant fees to the SBA to help offset what is perceived to be the credit subsidy cost necessary to underwrite the program. The Fiscal Year 2002 budget seeks to increase the fees paid by borrowers and lenders to offset the need for an annual appropriation.

We're aware of OMB's interest in making these programs self-financing. However, existing fees already offset the cost of the 7(a) program. The net result of increasing fees as proposed would be to drive both the small business borrowers and the lenders from the program. Every year, more than 40,000 small business applicants turn to the 7(a) program for their critical financing needs. These small businesses are unable to obtain comparable credit elsewhere. The increased fees being proposed would jeopardize needed credit to small business at the worst possible time as our economy has slowed dramatically and small business lending has become more difficult. We are also hearing complaints about the 50 basis point annualized servicing fee, which is applied to the outstanding balance of SBA's guaranteed portion of the loan and charged to lenders.

Obviously, in the next budget cycle, new and higher fees could again be proposed. To deal with some of these issues on a more permanent basis a few suggestions would be:

1) Congress should pass legislation prohibiting USDA and SBA from raising loan fees without approval from Congress;
2) Establish a large pilot program that would eliminate lender and user fees on small business loans in rural areas;
3) Increase funding for B&I and SBA loan programs;
4) Make SBA loan programs and related information available through USDA loan offices since USDA has a physical infrastructure in rural areas that SBA does not.

We point out that some of the demand for small business loans in rural areas is limited due to high fees. Eliminating these fees would attract greater participation and enhance the strength of the portfolio and the viability of the program as a whole. If the fees are too high, only high risk ventures will seek financing through SBA, thus increasing SBA's potential for losses.

Greater Broadband Capacity in Rural Areas -- We also need to find the right mix of policies that will spur greater investment in telecommunications technologies in rural America to help us bridge the "digital divide" between our rural and urban areas. Not only do we need to create more jobs in rural areas, we need to ensure that rural areas have access to the latest technology to make them less isolated from larger metropolitan areas and to attract people with the kind of leadership and job skills necessary to help our rural areas survive and thrive. In my community of Cando, our economic development council believes that our future rests with our ability to compete in the new economy. We need the technological infrastructure to line up at the starting gate.

Establishing New Programs

Mr. Chairman, the Center for the Study of Rural America, headquartered in the Federal Reserve Bank of Kansas City, is a national rural outreach committed to illuminating the issues and challenges facing rural America. In their recent national conferences, the Center has begun exploring the need to outline a broader rural policy that goes beyond farm policy.

One issue in particular the Center has examined is the need to bring more sources of equity capital to rural America to complement the debt financing offered by private-sector lenders. In 1999, the Center issued a report on the proceedings of their national conference entitled *"Equity for Rural America -- from Wall Street to Main Street."*

Some of the conclusions of this conference were summarized as follows:

- Few companies with high growth potential are located in rural areas;
- Some initial public funding for rural equity projects is necessary because returns are too low to attract venture capital investments to small rural companies;
- A greater degree of management assistance is likely needed for rural firms;
- Urban areas can attract equity capital much more efficiently than rural areas;
- Investors naturally migrate to larger deals;
- The key question – what degree of emphasis will be placed on economic development in rural areas versus earning a high rate of return?;
- An equity capital fund's goals and its institutional structure have a big impact on which deals are funded and how the fund exits from those investments;
- Creating local wealth that is locally controlled should be an essential goal;
- **A double-bottom line is needed** – both a good rate of return but also providing the rural communities with a major economic boost (jobs, etc);
- Community banks can play a vital role in leveraging the capital resources of local businesses; and
- Any serious attempt to boost the supply of equity capital in rural America has to include banks in the plan.

Rural Equity Fund -- The ICBA has worked with a coalition of organizations on legislation that would create a "rural equity fund" to help spur business development in these rural communities. There are about 3,000 rural banks considered by the Federal Reserve to be "agricultural banks" and many others that don't meet the definition of an "agricultural" bank are located in rural areas and make a considerable number of loans to consumers and small businesses on Main Street. Rural community banks need to be a part of the rural development equation.

The purpose of the "rural equity fund" again should be to encourage private investment in value-added agriculture enterprises and small business start-ups and expansions. Not all rural businesses will be "value-added" in terms of enhancing farm income from processing their commodities into food and other uses. A healthy rural community obviously needs many types of rural businesses. This includes both cooperatives and non-cooperative businesses and both large and small businesses, and credit tools that encourage individual entrepreneurship. Unfortunately, large venture capital funds are not interested in focusing on rural America.

The legislation would create a public/private partnership designed to attract equity investment into cooperative and other business ventures in rural America. The Fund would provide equity financing to help complement loan packages put together by the private sector and projects brought to the attention of the Fund by sponsors, including cooperatives, lenders and community development groups.

The fund would be capitalized by investments from private sector institutions and the government would match these monies up to a specified level. Investments made by this fund will provide off-farm income, additional markets for agricultural products and new business opportunities in rural communities. However, again we contend that any new or existing rural development program needs to be targeted *primarily* to truly rural communities based on population so we can diversify rural America's economic base.

By investing in an equity fund, rather than individual projects, private sector lending institutions would also avoid the mixing of banking and commerce, which is prohibited by Federal law.

Conclusion

Mr. Chairman, we appreciate the Committee's efforts. Strengthening the agricultural economy and creating business investment opportunities in our rural communities is key to a viable future for many family farmers and local area businesses. ICBA and its Agriculture-Rural America Committee look forward to working with the Congress to accomplish these goals. Thank you.

Testimony of

David Reis
American Premium Foods Co-op

Before the

Subcommittee on Rural Enterprises, Agriculture and Technology
Committee on Small Business
United States House of Representatives

Concerning

Value Added Incentives for New Generation Co-ops

Presented

July 17, 2001
Washington, DC

Chairman Thune, and members of the committee:

My name is David Reis. I am a pork producer and a fifth generation family farmer from Ste. Marie, Illinois, which is located in the far southeastern part of the state. I am currently serving as President-elect of the Illinois Pork Producers Association as well as a volunteer consultant to, and a member of, American Premium Foods Co-op. It is an honor to appear before this subcommittee on behalf of the over 240 independent pork producers that make up our newly formed cooperative to share with you some thoughts on what we are trying to accomplish in order to survive in this ever changing agricultural industry.

Like many industries in this country, agriculture is truly going through a period of extensive change and consolidation. The result is the traditional family farm is giving way to a system of contracted and integrated corporate operations. Studies predict that by 2007 the so-called "free markets for U.S. commodity hogs" will have all but disappeared. This means that the stand-alone producer of live commodity hogs will be reduced to reliance on "spot" markets that open and close as supply and demand dictates.

Some producers and organizational groups have resorted to spending their time and resources trying to stop this trend by asking for moratoriums and various price control measures. We in American Premium Foods have chosen another route. We have chosen to be proactive and engage in activities that will allow us to not only control our own destinies, but also to create more jobs and preserve rural economic activity as well. In our industry, the only way for family farms to survive this consolidation is for them to coordinate and capture the profits from processing their current commodity – live hogs – into value added food products. We must stop selling just hogs and begin marketing pork.

American Premium Foods Co-op was organized in late 1999 after almost a year of business plan development and membership recruitment by its founding leadership. As I stated previously, the co-op is currently comprised of 240 independent pork producers from throughout Illinois. We plan to construct a pork packing and fresh processing facility that is capable of handling 2800 head per day on a single shift basis. The plant will be the most automated and sanitary slaughter plant in the United States with our facility even meeting the tough European Union standards which are among the most stringent in the world. Our meat will be marketed under the newly formed *Meadowbrook Farms* label of which American Premium Foods Co-op owns a fifty-one percent majority of the shares.

Each carcass will be individually tracked through the plant and producer members will be paid for the wholesale value of the primal cuts from their hogs. The profits from additional processing will be paid according to the producer's percentage ownership in the plant.

Our $30 million facility will employ 210 people and have an annual payroll of approximately $6 million. Because of its small size the plant is designed to be an environmentally friendly asset to the community in which it is built. Currently the board of directors and its site selection committee is focusing on three to four sites to gather additional information.

In March of this year, *Meadowbrook Farms* announced the selection of its new National Sales Manager – Joe Leathers who was previously with PIC America and prior to that was in charge of demand enhancement with the National Pork Producers Council. Joe's been in the meat industry for a number of years but has had to always market meat from an existing plant or facility. What intrigued Joe about coming on board with our project was the fact that he could develop a marketing plan and then help design and build a plant around this marketing plan.

We have received much support from various state agencies and groups as our project has continued to evolve including the Department of Commerce and Community Affairs, Illinois Department of Agriculture, Illinois Pork Producers Association, Illinois Institute for Rural Affairs, University of Illinois, and many state and local farm organizations. In addition, the State of Illinois appropriated $1.7 million to our project and we were chosen just two weeks ago to receive a $500,000 grant through the USDA Value-added Agriculture Product Market Development program.

Our project, however, has not been without its share of frustrations and attacks from industry critics. Because we are the first venture of this size and scope in the nation, we had no business model to follow. It was deemed a "high risk" startup. We were advised by some to beware of the "snake oil salesmen." Most pork producer's equity and ability to invest in such a project was wiped out during the 1998 hog market crash. As you can tell it was very easy for the skeptics to sit back and take snipes at what we were trying to accomplish. However, the group held its course and continued to believe that what it was trying to do was worth fighting for because what was truly at stake here was the future of their independent pork operations and the backbone of most rural communities in the Midwest.

Everyone from the local extension offices to the halls of congress is promoting value-added, value-added, value-added. But I can speak from experience that it's not that easy and these projects just don't happen overnight. We at American Premium Foods have been working on this project for well over two years now and while the commitment from our board and its membership has been rock solid, as each day passes the integration and consolidation continues. Just a few weeks ago it was announced by Seaboard Corp. that they were terminating their plans to build a pork processing plant in Kansas which further confirms that most of the growth incurred by the major packers is through acquisitions and mergers rather than by investing in new facilities. And we've all seen in recent months with the high cost of gasoline and fuel what happens when an industry stops investing in itself.

So what can congress do to help? We need common sense solutions and assistance if more projects such as ours are going to successfully maneuver through the critical period of planning and startup. Weather it is pork or beef packing plants, soybean crushing, ethanol production, aquaculture, or one of many other value-added concepts being discussed, often time the difference between success and failure is the amount of time and money spent doing the preliminary work. These ventures need assistance in hiring the best firms to conduct the feasibility studies, the engineering, the marketing and business plan development and so on. We in the pork industry know how to raise pork better and more efficiently than anyone in the world but we need a little boost in helping us become better business owners in a broader sense when it comes to ventures as large as this.

This is why we are so excited about Congressman Thune's Value-Added Agriculture Package. We feel that both HB 1093 and HB 1094 will address two major hurdles co-ops face as they develop from the initial vision stages all the way to becoming a profitable venture for its members.

We can't begin to explain how many dead end roads we went down, programs we found out about after the fact, or just how many ideas we could have used from the beginning to help us get to where are much faster and with a lot less frustration. Individually ran co-op development centers are desperately needed because of the extreme complexity of rules and programs that are available in each state. They also need to be relatively close in proximity for travel purposes for its leaders as all startups are on a shoe string budget. In May of this year the Illinois legislature passed a bill which creates the AgriFirst program to assist value-added co-ops in getting started. HB 1093 will certainly complement AgriFIRST and fund it at a much higher level.

The tax credit language contained in HB 1094 will put incentives were they can do the most good. In established projects that have come to fruition and will enable the participating members to recover more quickly their initial capitol investment which will in turn make the co-op more profitable which will in turn allow the members to reinvest these profits back into in their communities. And that's part of why we are here today.

These are both excellent bills. I'm sure that most if not all, of the commodity groups will be in strong support of this legislation and they will really make a difference in what we are trying to accomplish in rural America.

From a Small Business Administration standpoint our co-op, because of its size, does not qualify for most of its loans. Lenders tend to ask us to focus on the various loan programs available through the USDA because the bulk of the programs offered by the SBA are geared for much smaller projects. Another suggestion would be for all government agencies to to a better job of marketing their programs to rural America and to perhaps cross sell all programs when a project doesn't qualify loans they have available.

In closing, Mr. Chairman and members of the committee, the producers in our co-op have agreed to lay their operations on the line and invest what little capitol they have left into this project. The future of independent pork production and a key ingredient in the sustainability of the rural landscape depends upon our success. Our industry is changing rapidly and by collectively working together we can find common sense ways to preserve the livelihood of independent farmers throughout the country.

Thank you Representative Thune for inviting me here to speak today. It was truly an honor and I look forward to answering any questions that the committee might have.

Statement by the

NATIONAL CATTLEMEN'S BEEF ASSOCIATION

on

Value-Added Enterprises

Submitted to the

House Small Business Committee
Subcommittee on Rural Enterprises and Agricultural Policy

The Honorable John Thune, Chairman

by

Mr. Jay Truitt
Washington D.C.

July 17, 2001

Chairman Thune and Distinguished Members of the House Small Business Committee:

On behalf of the National Cattlemen's Beef Association (NCBA), which is the trade association of America's cattle farmers and ranchers, and the marketing organization for the largest segment of the nation's food and fiber industry, thank you for your interest in NCBA's comments regarding value-added enterprises. I appreciate the opportunity to share with you the giant progress NCBA has made in this area, as an effort to respond to consumer's needs which also simultaneously has increased demand for our products.

Seventy percent of total U.S. beef volume is sold at the retail level, making the retail customer a key component to building demand and growing beef's market share. However, because of consumers' changing lifestyles and increased food options, meeting consumer needs is becoming more challenging for the fresh meat industry.

The U.S. beef industry's ability to stabilize consumer demand for beef was the result of diligent planning, persistence and focus. The industry has seven straight quarters of increased beef demand under its belt and has an aggressive long-range plan to keep demand and profitability growing. Increased consumer spending and per capita beef consumption have contributed greatly to the health of the U.S. beef industry.

According to Cattle-Fax, a private market research firm, consumer expenditures for beef topped $52 billion in 2000 – the first time ever annual spending exceeded $50 billion. Yearly per capita consumption of beef is projected to reach 66.2 pounds, while per capita consumption for pork and chicken totaled roughly 50.5 and 55.8 pounds, respectively.

Today this industry is one of the most dynamic segments of the U.S. agricultural economy, and we're just getting started. We've set an aggressive goal to boost demand another 6 percent through 2004.

The beef industry and industry partners began laying the ground work in the mid 1980s by emphasizing improvements in product consistency, tenderness and overall quality; new product development; enhanced relationships with channel marketing partners; multiple beef safety intervention measures; the opening of export markets; and research into beef's nutritional values and benefits.

A focus on adding value led to the formation of a long-range plan that concentrated all industry segments on a single goal – stabilizing consumer beef demand. We had to leave traditional business practices behind and create a visionary plan that all segments of the industry could get behind – one that helped us compete in a new economy ruled by consumer spending power and brand appeal.

There is cooperation across business segments in the beef industry like never before. Beef producers and industry partners are working to produce high quality beef products that satisfy consumer needs.

Three years ago, through the use of checkoff dollars, NCBA helped promote a new category of fully cooked beef roasts, steaks and other entrees that could be heated in the microwave and ready to serve in about 10 minutes. Since then, sales of these types of products have increased 41.4 percent, and annual sales for the new category topped $84 million as of December 2000. The beef checkoff also addressed beef's market share in the value-added fresh category, deli category, frozen meal kits containing beef and value-added products for the foodservice channel.

Just three years ago heat-and-serve beef entrees were almost unheard of. Today 61 percent of supermarkets in the U.S. have a convenience section in their fresh meat case and this category represents $117 million. The New Product Development Team, organized only three years ago, supported more than 50 innovative beef product introductions in 2000 alone.

New product programs are funded by beef producers through their $1-per-head beef checkoff program and are managed for the Cattlemen's Beef Board and state beef councils by the National Cattlemen's Beef Association. The national beef checkoff is administered by the Cattlemen's Beef Promotion and Research Board. This 110-member board is appointed by the Secretary of Agriculture to oversee the collection of the $1-per-head beef checkoff, certify state beef councils, implement the provisions of the Federal Order establishing the checkoff and evaluate the effectiveness of checkoff programs.

From steak to burgers to beef stew, the beef industry continues its emphasis on new, convenient, branded beef products. Through the "Best New Beef Products Awards 2000", manufacturers are recognized for their successes and are encouraged to use the prize money to bolster continued research and development of new, convenient beef products. The Cattlemen's Beef Board and the nation's beef producers sponsored the contest through the $1-per-head beef checkoff.

The impact of these convenient, branded beef products is evident in both the foodservice and retail arenas. At retail, sales of branded, prepared beef items for the fresh meat case have grown more than 67 percent (or $47 million) in the past two years. At foodservice, operators and executives are turning to high-quality, convenient, labor-saving beef products to deliver greater economic value.

Several years ago, NCBA identified category management as a key tool to help build retail beef sales, and the association has been working with many of the nation's top retail companies to help them implement elements of this evolutionary business practice. Because category management must be focused on the consumer to succeed, NCBA conducts ongoing research to help its retailer partners understand how changing attitudes and behaviors are shaping the future of their businesses.

As consumers' lifestyles change, so do their attitudes about shopping for and preparing meals. Because of growing time demands and pressures, consumers are putting off dinner decisions until the last minute. According to NCBA research, two-thirds of dinner decisions are made the same day. Of those, 73 percent wait until 4:30 p.m. to decide what to have for dinner. This "4:30 dinner dilemma" is reflected in the growth of foodservice sales. In the past 10 years, more consumers have bypassed their local supermarkets for take-out meals, and the level of spending at restaurants has nearly doubled.

Recent partnerships with restaurants such as Taco Bell have resulted in increased sales and beef additions to their menu. This partnership has made it possible for consumers to enjoy tender, marinated steak at a fast food restaurant, again adding value at a previously unlikely venue.

The beef industry also continues to build an aggressive new product development effort dedicated to increasing the value of the chuck and round. The R&D Ranch is the creative and technical warehouse for the beef industry's new product development expertise and knowledge, which is shared with industry partners (consumer branded manufacturers and foodservice processors).

The R&D Ranch team helps industry partners identify new beef and veal product opportunities that will complement and grow their businesses. The team can show industry partners how to transform the chuck and round (which traditionally have been underutilized and more challenging to work with) to become part of great eating experiences. They also use market research to help partners develop products consumers want. Finally, the team helps coordinate sales and marketing efforts – from cooking instructions and packaging to public relations – to help facilitate market success.

Each new development in the value-added arena helps facilitate small businesses competing both nationally and globally. NCBA strongly supports the passage of interstate meat shipment, which would enable producers to add value to commodities and ship product across state lines, and all over the world. This will continue to encourage niche marketing and value-added processing.

We also strongly support your efforts, Mr. Chairman, to further progress for value-added enterprises by providing grants to assist value-added agricultural business in such areas as technical assistance, applied research, market development, business planning and overall organization. Additionally, investment tax credits, under legislation you have sponsored, will provide even more incentive for producers to add value to commodities.

Thank you Mr. Chairman for the opportunity to visit with you and the House Small Business Committee today. I will be happy to answer any questions you or the Committee may have.