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Foley's Quarterly Food Industry Web Conference Series

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Today's Presenters



Scott Early
Chicago



Kathryn Trkla
Chicago



Holden Brooks
Milwaukee



Joyce Gresko
Washington, D.C.

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The Ongoing Impact of the Commodity Exchange Act on the Food Industry

Scott Early and Kathryn Trkla

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CEA Jurisdiction Over Derivatives

- The CEA regulates transactions and markets, with an emphasis on exchange markets, in:
 - “contracts for the sale of a commodity for future delivery,” called “futures contracts”
 - options on commodities
 - options on futures contracts
- Exchange-trading requirement for futures and options on futures, absent an exemption or exclusion
- Commodity options may be traded on or off-exchange

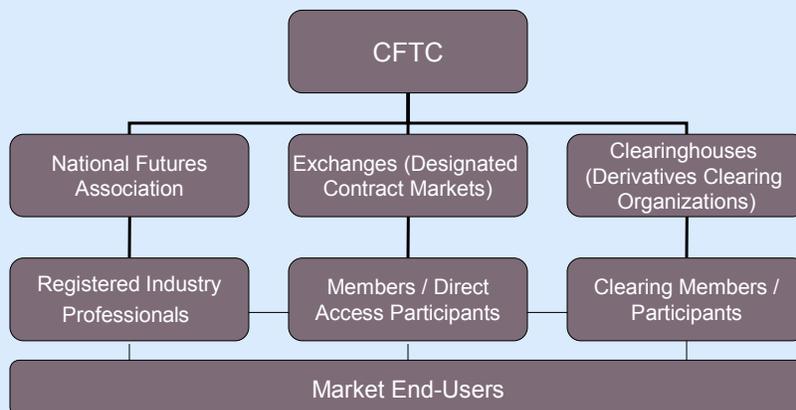
CEA Jurisdiction: Covered Commodities (Since 1974)

- Wheat, cotton, rice, corn, oats, barley, rye, flaxseed, grain sorghums, mill feeds, butter, eggs, Irish potatoes, wool, wool tops, fats and oils, cottonseed meal, cottonseed, peanuts, soybeans, soybean meal, livestock, livestock products & frozen concentrated orange juice (“***enumerated agricultural commodities***”), and
- “***all other goods and articles...and all services, rights, and interests in which contracts for future delivery are presently or in the future dealt in.***”

CEA Oversight Structure

- Administered by the CFTC (formed in 1975)
- Self-regulation by the NFA, exchanges & clearinghouses
- Primary Congressional oversight committees:
 - Senate Committee on Agriculture, Nutrition & Forestry
 - House Committee on Agriculture

Regulatory Framework



Regulation of Exchange Market Users (Selected)

- Position limits/position accountability
 - Set by the exchanges
 - Also set by CFTC for **wheat, corn, oats, cotton, soybeans, soybean meal and soybean oil**
 - CFTC proposed limits for certain energy commodities
- Hedge Exemptions from position limits
- Large trader reporting (CFTC Form 40)
- Ban on manipulation & attempted manipulation, **extends to the cash market**

OTC Derivatives - Exclusions / Exemptions from Exchange-Trading and Other Requirements:

- Forward contract exclusion for deferred delivery merchandizing transactions
- CEA exemptions for transactions between “eligible contract participants;” **not available for agricultural commodities**
- CFTC Part 35 exemption for transactions between “eligible swap participants;” **available for swaps and (commonly accepted) swaptions – but not options -- on agricultural commodities**
- CFTC Part 32 Options Rules; relevant primarily for ags

OTC Derivatives Legislation

- House Bill (December 2009)
- Senate Banking (Dodd) & Ag Committees
- Themes:
 - Prevent systemic risk: clearing of standardized contracts; oversight of swap dealers & major swap participants
 - Market transparency and efficiency: position reporting & limits; centralized trading of standardized instruments

Understanding the FDA's Reportable Food Registry

Joyce Gresko

What is the Reportable Food Registry?

- An electronic portal where information about possibly adulterated foods is submitted by “Responsible Parties”
- Found at www.rfr.fda.gov
- Purpose
 - Help FDA track patterns of adulteration in food
 - Help FDA target its limited inspection resources
- Part of the 2007 Food and Drug Administration Amendment Act, PL 110-85
- Went into effect September 8, 2009



What is a Reportable Food?

- Definition: “An **article of food** (other than infant formula) for which there is a **reasonable probability** that the use of, or exposure to, such an article of food will cause **serious adverse health consequences or death** to humans or animals.”
- Animal feed is included; dietary supplements are not.
- Class I recall food = Reportable Food
- Class II recall food may also be a Reportable Food, depending on the circumstances

Who is a Responsible Party?

- Definition: “A person who **submits the registration** under Sec. 415 of the FDCA for a **food facility** that is required to register, at which such article of food is **manufactured, processed, packed, or held.**”
 - In other words, the owner, operator, or agent in charge of a food facility.
- It is permissible to authorize another individual to make a Reportable Food report – it need not be the same person who submitted the registration.

What is a Responsible Party responsible for?

- **Reporting** through the Reportable Food Registry as soon as practicable, but in no case later than 24 hours after determining that an article of food is a Reportable Food
- **Getting a unique identifier** from FDA for the Reportable Food
- **Investigating** the cause of the adulteration if the Reportable Food may have originated with the Responsible Party
- In some cases, **providing notification** to immediate previous sources and subsequent recipients of the Reportable Food, after consultation with the FDA
- **Providing amended reports**, as necessary
- **Consulting** with the FDA to follow up, as necessary

A Responsible Party does NOT have to submit a report when...

- The adulteration originated with the Responsible Party AND
The Responsible Party detected the adulteration prior to any transfer to another person AND
- The Responsible Party corrected the adulteration or destroyed the adulterated food.
- All three criteria must be met, and be mindful of whether there has been a “transfer to another person.”

What information is included in a Reportable Food report?

- Food facility **registration number**
- **Date** the article of food was determined to be reportable (this could be the date that a contamination test was confirmed positive)
- **Description** of the food, including quantity and amount
- **Extent and nature** of the adulteration
- **Results of the investigation** and the cause of the adulteration if it may have originated with the Responsible Party, when known
- **Disposition** of the article of food, when known
- **Product information** typically found on packaging sufficient to identify the article of food (e.g. – use-by dates, name of the manufacturer, lot number)

What happens after a report is made?

- FDA reviews the report with the Responsible Party.
- FDA may require the Responsible Party to amend the report.
- FDA may require the Responsible Party to notify the immediate previous source(s) and immediate subsequent recipient(s) of the adulterated food.
- Responsible Parties also are encouraged to contact their local FDA offices and/or public health officials about the adulterated food.

Record keeping requirements

- Responsible Parties must maintain records for **two years** of
 - Reports made
 - Reports received
 - Notifications made to third parties
- FDA may inspect Responsible Parties' records.
- Reports are available for public disclosure under the Freedom of Information Act (except for registration numbers, location and identity of registered persons, trade secrets, etc.).

Antitrust Update: Developments Affecting the Food Industry

Holden Brooks

Overview

- Antitrust enforcement is up in all industries
 - Obama administration has vigorously challenged mergers, pursued enforcement initiatives
- But food/agriculture has been one of the top priorities
 - USDOJ/USDA workshops
 - Investigations
 - Merger challenges

USDOJ/USDA Agriculture Antitrust Workshops

- Announced in August 2009
- Will take place over 2010
 - March workshop in Iowa on farming issues
 - May workshop in Alabama on poultry issues
 - June workshop in Wisconsin on dairy issues
 - August workshop in Colorado on livestock issues
 - December workshop in DC on margins

Unprecedented Attention to Agriculture and Antitrust

- Significant outlay of USDOJ and USDA resources
- Coverage in business, agricultural press
- Over 15,000 public comments, including significant initial comments
- Attorney General Eric Holder at initial workshop
- Antitrust head Chistine Varney pledged an "unrelenting quest to find the correct balance" within the agricultural industry.

Context of Workshops

- Bush Administration more hands-off approach to antitrust enforcement
- Coincided with advances in technology, increased concentration, and vertical integration that changed competitive environment.
- Also coincided with judicial narrowing of antitrust laws.
- Perfect storm for uptick in enforcement.

Context of Workshops, cont.

- Potential need for enforcement at several points in the “food chain”
 - Inputs
 - Buyers
 - Processors
 - Retailers
- Idea is to combine USDOJ and USDA powers
- Focus is farming, but ultimate target is food prices

March 13, 2010, Iowa Workshop

- Topic was general farming issues, but focus was seeds
- Followed USDOJ stepping up Monsanto investigation
- Holder and Varney indicated that status of IP on seed traits, introduction of generics, would be focus of future enforcement

Seed-related Antitrust Issues

- Monsanto has patents on “Round-up Ready” seed traits, genetic modifications
- Allegation is that prices, restrictions have increased over time as competition has allegedly diminished.
 - USDA estimate is 56% increased cost of seed since 2006
 - Four seed companies account for 50% of worldwide seed sales
 - In US, 92% of soybean acres are planted with Monsanto seed and 80% of corn acres
 - Monsanto estimates farmers have seen extra \$20 billion in income, and also challenges the factual bases for the arguments re dominance and harm to innovation and competition
- Alleged that cost of seed trickles up to increase food prices

IP/Antitrust Intersection

- Attorney General Holder signaled at March workshop that IP rights may be challenged
- Fight may be centered on whether competitors can combine traits with Roundup Ready traits, or whether Monsanto can exclude based on IP
- Already significant debate in antitrust world
- Monsanto initial comment is extensive, lays out IP position and challenges argument that IP has reduced competition, underlying facts

May Workshop: Poultry

- Buyer power is primary focus, concentration among processors
- Anticompetitive effect of contracts also concern expressed in comments

June Workshop: Dairy

- Varney has already issued comments on dairy
- Congressional focus on antitrust enforcement in dairy industry
- Focus is on buyer power, alleged concentration among milk buyers
- Vertical integration of particular concern

August Workshop: Livestock

- Focus is on where antitrust law ends and USDA's enforcement of Packers and Stockyard Act begins
- Consolidation of processors is primary concern expressed in comments
- Some concern that all species should not be considered in same workshop

December Workshop: Margins

- Most theoretical, economics-based workshop
- Should focus on discrepancies between cost of producing food on farm, price earned by farmers, and end-user price for food
- Workshop could reach issues such as packaging and transportation

Feeser's RPA Case

- Third Circuit Court of Appeals 2010 decision
- Feeser's sued potato/egg product supplier, Michael Foods, for price discrimination under Robinson Patman Act
- Appellate court reversed district court, finding that Feeser's and Sodexho not similarly situated and did not compete "for same dollar" as required by RPA
- Feeser's sold food; Sodexho sold food services, which included purchasing

Bemis/Alcan Merger

- \$1.2 billion merger of food packagers
- In February 2010 settlement, DOJ insisted on divestment of cheese and meat packaging facilities; roughly 7% of assets
- Seen as part of trend of aggressive merger enforcement

Smithfield “Gun Jumping” Fine

- Smithfield and Premium Standard pork packers merged in 2007
- Post-facto, DOJ determined that they had collaborated prior to consummation of merger while they were still competitors
- Settled for \$900,000 in civil penalties in February 2010
- Sign of aggressive merger enforcement

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