

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MONTANA
BILLINGS DIVISION

RANCHERS CATTLEMEN ACTION LEGAL)	
FUND UNITED STOCKGROWERS OF)	
AMERICA,)	
)	
Plaintiff)	
)	Cause No. CV-05-06-BLG-RFC
v.)	
)	
UNITED STATES DEPARTMENT OF)	
AGRICULTURE, ANIMAL AND PLANT)	
HEALTH INSPECTION SERVICE, et al.,)	
)	
Defendants)	

DECLARATION OF FRANK FILLO

I, Frank Fillo, make the following representations based upon my personal knowledge and upon facts made known to me in my capacity as an official with the Animal and Plant Health Inspection Service (APHIS) of the United States Department of Agriculture (USDA).

1. I am the Assistant Chief and Supervisory Economist of the Policy Analysis and Development staff of APHIS. The Policy Analysis and Development staff provides the economic analysis required for rulemaking and assists APHIS decision makers in the evaluation of policy and program issues. I received a Bachelor of Arts degree in Social Sciences from the University of the Pacific in 1972, a Masters of Education in Earth Sciences from Pennsylvania State University in 1976, a Masters of Science in Agricultural Economics from the University of Nevada in 1978, and a Doctorate of Philosophy in Agricultural Economics from the University of Florida in 1984.

2. I was the lead economist in charge of the development of the economic analysis for the Minimal Risk Region rule. I was the principal author of the analysis and prepared all tabulated data. In drafting the economic analysis, I consulted with Dr. Ann Seitzinger, an economist with the Centers for Epidemiology and Animal Health, Veterinary Services, APHIS; Mr. Ronald Gustafson, an economist with USDA's Economic Research Service; and Mr. Shayle Shagam, an economist with USDA's Office of the Chief Economist. Dr. Seitzinger and Messrs. Gustafson and Shagam are experts in the field of livestock economics. The economic analysis was reviewed by USDA's Office of Budget and Program Analysis, the Office of the Chief Economist's Office of Risk Assessment and Cost-Benefit Analysis, and the Office of Management and Budget's Office of Information and Regulatory Affairs.

3. I have reviewed the Declaration of John J. VanSickle dated January 29, 2005, as well as the Amended Declaration of John J. VanSickle, which was also dated January 29, 2005, and which were filed by the plaintiff in this lawsuit.

4. Mr. VanSickle alleges that the discovery of BSE in a domestic herd causes a loss of consumer confidence in the safety of beef and a concomitant decline in domestic beef consumption. However, contrary to Mr. VanSickle's assertions, USDA data indicate that consumer demand for beef has remained strong in both Canada and the United States since the discovery of BSE in North America in 2003. Canadian per capita beef consumption increased by 1.1 kg in 2003 and U.S. demand in 2004 is estimated to have increased 7-8% over 2003 levels. It is important to note that USDA began issuing permits to allow the importation of certain beef products, including boneless beef derived from cattle less than 30 months of age, from Canada in August, 2003. The quantity of beef imported from Canada in 2004 (797 million pounds) represented 96% of average imports in the three-year period 2000-2002 (826 million pounds).

Thus, the United States has continued to import nearly as much Canadian beef since the discovery of BSE in North America as it did prior to this discovery, and this importation has not resulted in a loss of consumer confidence in the safety of the U.S. meat supply or a decline in domestic beef consumption. As noted by Colin A. Carter, professor of agricultural economics at the University of California, Davis, "Consumers in North America have not turned away from beef, because they may well recognize that the risk to them from a BSE-related death is close to zero & When the first case of BSE occurred in the United States, analysts believed that this incident would have a serious impact on the U.S. domestic beef market. Based on market reactions in Europe and Japan, a possible outcome in the U.S. would have been an excess supply of beef and lower domestic prices. So far, the overall market impact of BSE in the United States has been minimal & While it is difficult to speculate about the long-term effects of BSE, the history of other food safety scares and impacts on consumer demand in the U.S. has shown these scares to be rather short-lived." (Carter, Colin A. and Jacqueline Huie, "Market Effects of Searching for Mad Cows." Giannini Foundation of Agricultural Economics, University of California, Davis, ARE Update, Vol. 8, No. 1, Sep/Oct 2004, http://www.agecon.ucdavis.edu/outreach/areupdatepdfs/UpdateV8N1/V8N1_3.pdf.)

5. Mr. VanSickle cites the APHIS economic analysis for the proposition that the Final Rule will have a negative impact on cow-calf producers of \$2.5 to \$3 billion and that this will have a "devastating effect on already-weakened U.S. producers" which, he alleges, "have already suffered from a prolonged period of inadequate returns." (VanSickle Declaration ¶¶ 8, 17) APHIS estimation of producer losses includes other sectors of the livestock and meat processing industry in addition to cow-calf producers and is a projection of losses through 2009. Furthermore, there is strong evidence that U.S. cow-calf producers are not in a weakened

economic state. First, U.S. cow-calf producers have benefitted from the ongoing strong demand for beef, despite the North American BSE occurrences. Additionally, annual estimates of per cow cash returns over all cash costs (including interest, some hired labor, etc.) plus pasture rent (often producers own the pasture) for U.S. cow-calf producers from 1974 to 2004 have been positive for the past six years, reaching their highest level for the 30 year period of \$150 per cow in 2004. It is also important to note, and Mr. VanSickle concedes, that the economic analysis concluded that the rule would result in a net economic benefit of \$66-74 million through 2009.

6. Mr. VanSickle cites USDA's estimate that [c]onsumers of beef from steers and heifers are expected to lose \$76.3 million as Canada ships in less beef from steers and heifers and more beef from older animals for processed beef markets (VanSickle Declaration ¶ 9). On February 9, 2005, Secretary Johanns announced that the implementation of the provisions of the rule lifting the ban on the importation of beef derived from Canadian cattle slaughtered at greater than 30 months of age will be delayed. In the analysis, we assumed that there would be slaughter in Canada of cattle over 30 months of age in place of fed cattle under 30 months of age, making the displaced fed cattle available for importation into the United States. Because of the announced delay, USDA now expects fewer fed cattle to be imported into the United States because of the rule, and the rule's impact on cow-calf producers actually will be smaller than initially estimated.

7. Mr. VanSickle also states that the beef consumers who will benefit from the rule are fed-cattle consumers, that is, all operations and users that follow the feedlot operator (i.e., meat packers and large supermarket chains) (VanSickle Declaration ¶ 9), and that there would be little benefit to the individual U.S. consumer. While we can't say to what extent the expected benefits of the rule in terms of lower beef prices will reach the final consumer, it would be a

mistake to assume that all the welfare gains due to price reductions would be captured by the meat packers and supermarket chains. If they do possess some degree of market power in pricing beef, increases in the quantity of beef sold could induce them to increase their margins.

8. The amended Declaration of Mr. VanSickle states that USDA's economic analysis "ignores the impacts imports of beef and cattle will have on associated industries and their productive output, as well as the impact imports will have on employment" (Amended VanSickle Declaration ¶ 10). According to Mr. VanSickle, his economic model shows that a decline of \$1 in sales for the cattle ranching and farming sector will have a \$6.15 impact on total economic output and a \$2.97 impact on personal and business income. He also calculates that the rule will have "a total negative impact on U.S. economic output of \$4.07 billion a year, cost 40,850 American jobs and cause a negative \$1.96 billion income effect" (Amended VanSickle Declaration ¶ 10). APHIS clearly did consider the rule's impact on associated industries by performing a multi-sector economic analysis of the impact on the animal feed, animal production, and animal product processing sectors. This analysis projected modest declines (3.3-4.1%) in cattle prices for 2005, with concurrent declines of gross revenues for the cattle and beef industries (3.9-4.8% and 1.3-1.6%, respectively). However, it projected gross revenue declines of only 1.4-1.7% for the combined livestock, feed, and grain sectors. Therefore, there appears to be little spillover into other agricultural sectors. The model did not consider either the economic benefits or detriments which the economic activities of cattle producers and meat processors will have on their surrounding communities because the magnitude of the price and quantity changes found by the multi-sector analysis suggested that the rule would have little impact on U.S. wages, employment, or industry structure, at least on the national level. To the degree that the rule would impact wages and employment on a regional basis, wage and

employment levels in a given region still would be more strongly influenced by the general health of that region's economy and the resulting employment opportunities available in that region. This is consistent with the observed limited impacts of the initial closing of the U.S.-Canadian border from May to December of 2003.

Additionally, the analysis presented by Mr. VanSickle estimates only the negative impacts to the wider economy while ignoring its positive impacts. The rule will increase the total supply of cattle to the United States. During the first year the rule is in effect, the net increase in cattle slaughtered in the United States can be estimated to be about 795,500 head (fed cattle, 650,800 head, and seven-twelfths of the increase in feeder cattle, 144,700 head). When valued (conservatively) using a price of \$950 per head, these additional cattle generate \$755.7 million in additional sales. Applying Mr. VanSickle's choice of multiplier, these increased sales yield an economic gain of \$4.65 billion a year, more than offsetting his estimated loss of \$4.07 billion. Similarly, the increased sales will have a positive effect on employment and income, again more than offsetting the losses in employment and income estimated by Mr. VanSickle.

9. Mr. VanSickle surmises that the final rule likely will have a negative effect on U.S. beef exports. He states that U.S. beef exports declined 82.4% from 2003 to 2004, representing an annual loss of \$8.5 billion for the U.S. cattle industry in 2004, and that U.S. cattle prices would have been 12.8% or almost \$15/cwt higher in 2004 if U.S. export markets had not been closed due to the findings of BSE in North America. He predicts that continued and/or increasing declines in U.S. beef exports as a result of the rule could negatively impact the U.S. economy with a \$52.3 billion output effect, cost the economy 525,300 jobs and a \$25.2 billion income effect (Amended VanSickle Declaration ¶ 12). He further states, "If even one of our major trading partners chooses to continue banning U.S. beef as a result of its co-mingling with

Canadian-origin beef, the adverse economic impact will dwarf the modest net welfare gains predicted in USDA/APHIS economic assessment (Amended VanSickle Declaration ¶ 14). The approach Mr. VanSickle used is simplistic and doesn't fully account for all the changes taking place in the market place. With a decline in demand due to lost exports, price declines as there is excess supply on the domestic market. The decline in price then encourages domestic consumers to purchase more beef (increase domestic quantity demanded). Thus domestic consumers make up part of the lost exports. Conversely, if export markets were to reopen and foreign buyers quickly resumed their purchases there would be excess demand within the market. Prices would rise and domestic consumers would respond to this price increase by cutting back their purchases. As a result, total increase in meat consumed would be less than the increase in exports. Therefore, estimating changes based upon a price flexibility coefficient, as Mr. VanSickle does, overestimates expected changes in cattle prices, cash receipts, and employment.

A simple critique of the magnitude of Mr. VanSickle's trade estimates can be done by comparing his numbers to overall agricultural numbers. Mr. VanSickle claims that the change in total economic activity, i.e. gross domestic product (GDP), from lost beef exports could be \$52.3 billion. All of agriculture's contribution to GDP averaged \$72.6 billion from 2000 to 2002. Thus, Mr. VanSickle is claiming that continued lost exports as a result of allowing Canadian imports of cattle will reduce agriculture's contribution to the general economy by 72%. Similarly, Mr. VanSickle claims that allowing Canadian cattle to enter the United States will cost the U.S. 525,300 jobs. Analysts at USDA-ERS estimated that agricultural exports generated 808,000 jobs in 1998 (Rural America, page 58, May, 2001, USDA-ERS). As such, Mr. VanSickle is claiming that nearly two-thirds of these jobs are a result of beef exports. This is rather high given that the value of red meat exports (which includes pork and lamb) were less

than 10% of total agricultural export value in 2003. Also, Mr. VanSickle did not take into consideration employment gains from processing the additional cattle in U.S. slaughter plants. Currently, a number of U.S. meat processing plants have excess capacity. For instance, Tyson has suspended one or more shifts in five of its beef slaughtering plants due to lack of cattle to slaughter. We anticipate that the importation of Canadian cattle under this rule could help meet industry demand for additional cattle.

10. Regarding the Canadian restrictions on U.S. imports, Mr. VanSickle alleges, both in his original and amended declaration (which was not filed until February 8, 2005), that Canada currently prohibits the importation from the United States of cattle and most beef products. Further, he states that the final rule will allow imports of cattle and meat from Canada at the same time that Canada prohibits similar products being exported to Canada from the United States. First, it should be noted that Canada has never prohibited the importation of U.S.-origin cattle for slaughter, even immediately following the detection of a BSE-infected animal in Washington State. Furthermore, since April 23, 2004, Canada has allowed feeder calves to be imported from the United States. Second, it should be noted that the Canadian Food Inspection Agency issued proposed import regulations on January 31, 2005, which would significantly expand access for U.S. cattle and beef products. In fact, under these proposed regulations, Canada would allow the importation of live cattle born in 1998 or later, as well as beef from cattle of any age. Therefore, once these regulations become effective, Canada's import policies will be more liberal than those of the United States.

11. Mr. VanSickle also challenges USDA's assumption that the rule will result in no more than a 2% reduction in domestic demand, claiming that this assumption is inconsistent with the experiences of Canada, which saw a \$50/cwt decline in cattle prices following the discovery

of BSE there, and of Poland, which saw a 25% decline in beef consumption following the discovery of BSE in western Europe. He states that, if we assume a 2% decline in U.S. consumer demand results in a 0.5% decline in U.S. cattle prices, then a 27% drop in U.S. consumer demand, based on the experience of Poland, would cause a 6.75% drop in U.S. cattle prices and cost U.S. producers \$3.8 billion per year. Mr. VanSickle also cites a study by North Dakota State University (NDSU) which estimated that this impact could be as high as \$12.2 billion. USDA's assumption that U.S. demand for beef could decline 2% in response to consumer fears about the co-mingling of U.S. and Canadian beef was hypothetical, but it is not inconsistent with U.S. consumer behavior since the discovery of BSE in North America in 2003 or with current market expectations. As previously noted, USDA data indicate that consumer demand for beef has remained strong in both Canada and the United States. Given U.S. consumers' current lack of a negative response to the first cases of BSE discovered in the North American beef supply, USDA assumed that any negative response to the re-opening of the U.S.-Canadian border to beef imports from Canada would be modest. In contrast, the NDSU study cited by Mr. VanSickle takes as its starting point the assumption that there will be declines in U.S. beef demand due to consumer concerns about the safety of the U.S. beef supply. USDA's previously cited data on U.S. demand for beef since the discovery of BSE in North America effectively refute that assumption.

R-CALF's and Mr. VanSickle's drawing upon the experience of Poland and other countries following the discovery of BSE in their cattle populations to support their argument that the rule will depress U.S. consumer demand is misleading for several reasons. First, incidents of BSE have occurred in 20 European countries, as well as Japan, and the magnitude of the problem in Europe dwarfs the 4 occurrences observed in North America since 2003.

According to Great Britain's Department of Environmental, Food, and Rural Affairs, Britain had 180,687 confirmed cases of BSE as of January 1, 2005, which represents 95% of all BSE cases worldwide. It also had 147 confirmed or probable cases of vCJD between 1995 and September, 2004. In addition, the website for the International Office of Epizootics (OIE) indicates that the numbers of reported cases of BSE between 2000 and 2004 were 1,037 for Ireland, 119 for Belgium, 71 for the Netherlands, 865 for France, 351 for Germany, 122 for Italy, 123 for Switzerland, 570 for Portugal, and 509 for Spain. The OIE website also indicates that Poland reported 4 cases of BSE in 2002, 5 cases in 2003, and 11 cases in 2004, and it has already reported 2 cases in 2005. In light of this trend and the overall numbers for the rest of Europe compared to those for North America during the same time period, it is not surprising that consumers in Poland and the rest of Europe have had much stronger negative reactions to the presence of BSE in their cattle populations. Second, far less was known about BSE at the time these outbreaks were first occurring, stoking public fears and negative consumer responses. Thirdly, negative public and consumer reactions were exacerbated by the lack of transparency with which the governments of some countries, most notably Japan, initially handled their outbreaks. As a result, the experiences of these countries is not a good predictor of how U.S. consumers or our major trading partners will respond to an increase in Canadian-origin beef in the United States following implementation of the rule, especially given the vastly smaller numbers of infected cattle and the numerous mitigation measures in place in both countries.

12. Mr. VanSickle's declaration states that the adverse effects of the rule on U.S. producers could be mitigated *to some extent* by requiring labeling of beef from Canada and from Canadian-origin cows (VanSickle Declaration ¶ 18). Mr. VanSickle's comments regarding the mitigating effects of a country of origin labeling (COOL) program for beef imports from Canada

are speculative, based upon his explicit and implicit assumptions about the impact of the final rule on U.S. consumer demand for beef, and unsupported by any evidence. While APHIS did not consider COOL as a mitigating measure under this rule, USDA's Agricultural Marketing Service (AMS) has published a proposed rule establishing a mandatory COOL program for numerous commodities, including beef, in October, 2003. The proposal clearly stated that the intent of the COOL program "is to provide consumers with additional information on which to base their purchasing decisions. *It is not a food safety or animal health measure. COOL is a retail labeling program and as such does not address food safety or animal health concerns*" (emphasis added). Since the program does not address food safety or animal health, it falls outside the scope of APHIS authority and the scope of the Minimal Risk Region rule and APHIS did not consider it in the context of this rule. The program was supposed to go into effect in 2003, but Congress intervened by passing Public Law 108-199, which delayed implementation of the COOL program for all commodities except fish and shellfish until September, 2006. When implemented, the COOL program will require COOL for cattle and beef imported from Canada. In the meantime, APHIS does not consider it necessary to delay the implementation of the Minimal Risk Region rule until the COOL program is implemented.

As previously noted, Mr. VanSickle proffers no evidence in support of his contention that COOL would be an effective mitigating measure, nor does he acknowledge the costs of such a program. However, AMS did analyze the program's potential impact on the U.S. economy, including the cattle and beef sectors. It determined that the impact of the program would fall disproportionately upon the cattle sector. AMS also evaluated several studies of the first year costs of the COOL program, including one by Mr. VanSickle, and determined that cattle and calf producers' start-up and maintenance costs for record-keeping during the first year of

implementation would be \$61,847, 680 and \$133,951,509, respectively, for a total of approximately \$196 million. AMS also estimated the impact of the COOL program on U.S. prices for cattle and beef and on levels of U.S. production, exports, and imports of those commodities. It found that U.S. prices for cattle would increase 3.7-17.76 cents per cwt and U.S. prices for beef would increase 0.24-0.92 cents per pound; that U.S. production of cattle would decline by 48-112 thousand head annually and U.S. production of beef would decline by 39-88 million pounds annually; that U.S. exports of beef would decline by 3-10 million lbs. annually; and U.S. imports of beef would decline by 3-8 million lbs. annually. Compared to these costs, AMS determined that the estimated benefits of COOL were likely to be negligible. It also found little evidence that U.S. consumers have a strong preference for country of origin or that COOL would increase U.S. demand for food items bearing U.S. origin labels. It concluded that the compliance costs of the COOL program would be the driver of the aforementioned rise in U.S. prices, that U.S. consumers would not be willing to pay a price premium for COOL, and that U.S. producers would not be able to recoup their program costs.

13. Mr. VanSickle also states, [A]llowing processors to test animals they slaughter for BSE *would appear* also to mitigate *somewhat* the adverse effects of allowing Canadian imports, but USDA did not assess the costs and benefits of that option, either (VanSickle Declaration ¶ 18). Here again he makes an assertion which is purely speculative and unsupported by any evidence whatsoever. Furthermore, Mr. VanSickle completely ignores the enormous costs that would be imposed on the industry and consumers resulting from a testing program that has no basis in science. USDA is authorized to use testing for BSE and other animal diseases to promote and protect human and animal health in the United States, and any other use of such testing falls outside the scope of its duties. Therefore, USDA did consider the mitigating effects

of voluntary testing of cattle for BSE, but only in the context of safeguarding human and animal health. In the comments section of the Final Rule, APHIS responded to R-CALF's argument as follows:

APHIS has considered carefully the possibility of allowing private companies to conduct their own BSE testing, and remains convinced that *allowing such testing for private marketing programs is inconsistent with USDA's mandate to ensure effective, scientifically sound testing for significant animal diseases and to maintain domestic and international confidence in U.S. cattle and beef products. . . . [W]e consider it important to maintain clarity with regard to the purpose of USDA's BSE testing and the results such testing yields. . . . [C]urrently available post-mortem tests, although useful for disease surveillance, are not appropriate as food safety indicators* (emphasis added).

Elsewhere APHIS addressed the testing of ruminants generally as follows:

Development of reliable food safety indicators will require improved understanding of the pathogenesis of the disease and improved laboratory methods. . . . *Testing of individual animals, especially if it is performed on clinically normal animals at slaughter, is not in itself an effective risk mitigation measure for protecting public health. The purpose of a surveillance program is to gauge the level of BSE prevalence. . . . For these reasons, we do not consider the testing at slaughter of every bovine over 20 months of age, or the testing of every bovine at slaughter, to be scientifically justified or meaningful in the context of either human or animal health. Making this a criterion for minimal-risk regions would not contribute to human or animal health protection beyond the protection achieved by a statistically and epidemiologically valid surveillance plan, coupled with the risk mitigations specified in this rule* (emphasis added).

I declare under penalty of perjury that the foregoing is true and correct.

Executed on _____ at _____.
