Marketing Orders and Brand Promotion… Got (Milk) Lawyers?

by

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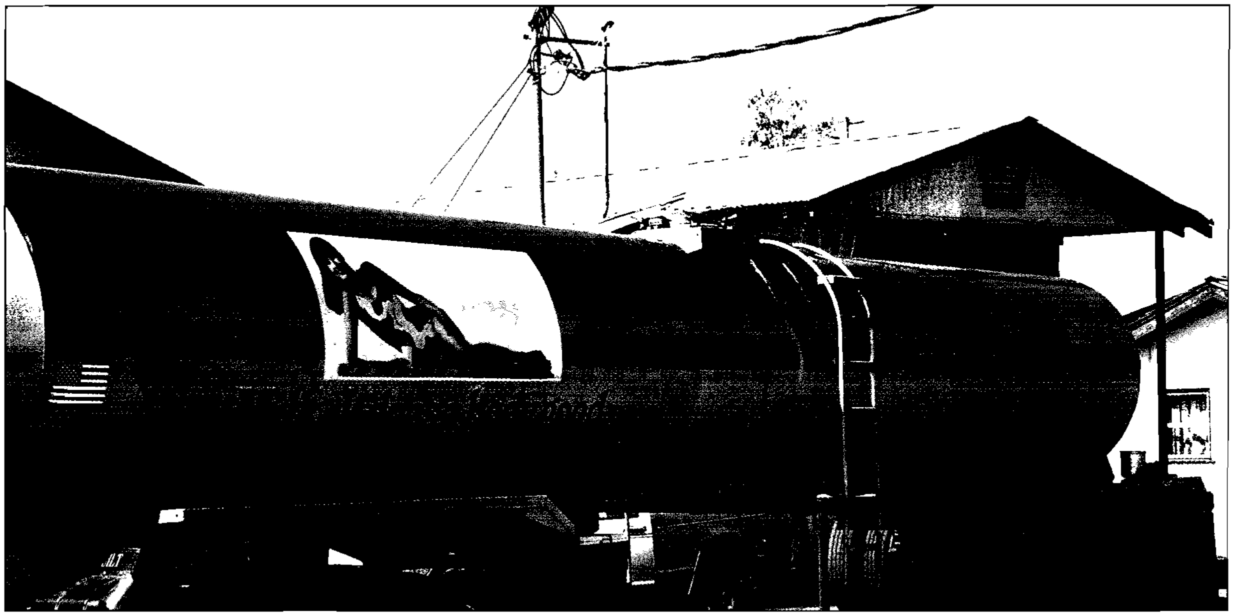
Got Lawyers?



To market or to court.... The current "Got Milk?" campaign and its predecessor, depicted here on a bulk tanker loading at a dairy in Chino, CA, are perhaps the most well-known commodity promotion campaigns. Litigation involving marketing orders and promotional programs for other crops and commodities pose a potential threat to the viability of these types of marketing activities.

Clear Window photo

Marketing orders were supposed to raise the tide for the entire industry, but some producers say it's not what floats their boats.

BY JOHN M. CRESPI AND RICHARD J. SEXTON

Many agricultural industries promote their products with funds generated from mandatory contributions by producers and/or handlers. Studies have shown that these programs often yield an excellent rate of return. Nonetheless, these programs have been controversial, and have endured numerous legal attacks on the grounds that they violate participants' First Amendment rights by compelling them to associate with competitors and support advertising messages with which they disagree.

Most observers believed that the Supreme Court had ended litigation, at least on First Amendment grounds, by ruling in favor of the marketing programs. However, a November 1999 decision by the U.S. Sixth Circuit Court of Appeals threatens to reignite the debate.

Although some have dismissed the issues represented in the cases described here as the result of free riders, free-market extremists, or unbridled lawyers, the concerns go much deeper. In some ways they reflect modern agricultural marketing, in which the goal is to highlight product quality and to differentiate products previously treated as homogeneous commodities.

Future challenges to commodity advertising programs may take place both in the courts and within the commodity organizations that administer the marketing orders. To help insure the vitality of these generally beneficial programs, it is useful to explore the concerns raised in the litigation and to design marketing programs that reflect these concerns.

Marketing Orders: A Timeline

1937: **Agricultural Marketing Agreement Act (AMAA)**

1930 *1940*

From Legislation to Litigation

The Agricultural Marketing Agreement Act of 1937 (AMAA) provided the statutory authority for marketing orders. The timeline along the bottom of pages 18–23 provides a timeline of key events relating to promotion activities funded under these programs.

In 1954 Congress amended the AMAA to authorize "marketing development projects," that would further the goals of the original Act. After two Supreme Court decisions, *Abood v. Detroit Board of Education* and *Central Hudson Gas & Electric v. Public Service Commission of New York*, clarified First Amendment rights in cases unrelated to agriculture, opponents of these commodity programs saw an opportunity to challenge them on constitutional grounds. (See the following sidebars for brief descriptions of these cases).

United States v. Frame represented the first key test coming from agriculture. The complainant, who raised beef cattle, argued that the marketing order amounted to

Heard it through the.... The table grape industry in California is just one example of a segment that has benefitted by collective promotional efforts.

From *Abood* to *United Foods*: A Brief History

The first cases that bore on the First Amendment issues embodied in the marketing order cases had nothing to do with agriculture: *Abood v. Detroit Board of Education* and *Central Hudson Gas & Electric v. Public Service Commission of New York.* However, the decisions in these cases formed the framework for testing the constitutionality of marketing order programs. Following is a description of Abood and Central Hudson, along with outlines of the major marketing order cases: Frame, Cal Almond, Wileman, and United Foods.

The *Abood* case began in 1969 and involved a collective bargaining agreement between the Detroit Federation of Teachers and the Detroit Board of Education requiring nonunion teachers to pay a service charge equal to the regular union dues. Some teachers objected, arguing that they were compelled to associate with an organization and finance ideological and political speech with which they disagreed in violation of their First Amendment rights.

The Court ruled that a government deeming labor relations to be important for a healthy economy can compel payment for collective bargaining. However, the union could not fund speech unrelated to collective bargaining or related issues using an individual's dues or service charges, if that individual disagreed with the viewpoint expressed.

During the energy crisis of 1973, the Public Service Commission of New York ordered electric utilities in New York State to suspend all advertising that promoted electrical usage. Central Hudson Gas & Electric Corp. opposed this ban on First Amendment grounds. The Supreme Court decided *Central Hudson Gas & Electric v. Public Service Commission of New York* in June 1980 (447 U.S. 557). In doing so, the Court set up the so-called "three-prong test" that must be administered in appropriate commercial speech cases:

First, does the program involve a substantial government interest?

Second, does the regulation directly advance that governmental interest?

Third, is the government's program narrowly tailored to minimize adverse impacts on First Amendment rights?

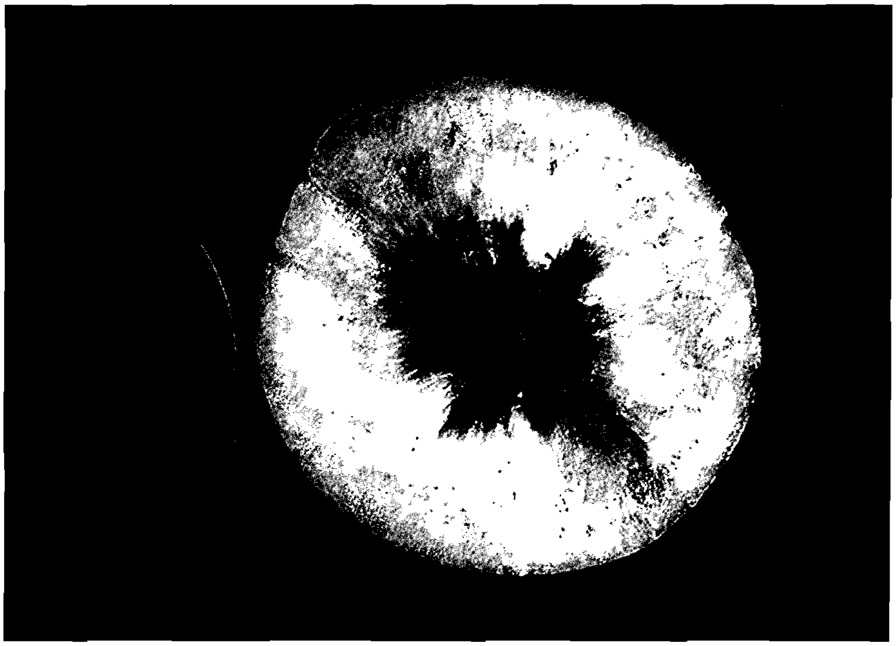
Failure on any one of the three prongs renders the regulation unconstitutional.

1954: **Congress amends AMAA to allow "marketing development projects"**

1950

Not exactly peachy: At issue in Wileman Bros & Elliot, Inc. was the Califonia Tree Fruit Agreement, covering the marketing of the state's nectarine, plum and peach crops

Photo courtesy of USDA/ARS



compelled speech and compelled association. The Third Circuit Court of Appeals found that there was a First Amendment implication in *Frame*, but the Beef Promotion Act itself was constitutional because it met several court-defined tests: it served compelling state interests, was ideologically neutral, and its goals could not be achieved through means with less impact on free speech or free association rights.

The next challenge, involving California almonds, began in 1987. Under the federal marketing order for almonds, handlers who advertised their own products could be reimbursed for their promotion assessments, provided that the advertising met requirements set by the Almond Board. Some handlers believed that these requirements favored the Blue Diamond Growers cooperative, the largest marketer of almonds, and holder of a majority vote on the Almond Board at the time. The courts (see the sidebar on p. 21) ultimately agreed with the plaintiffs, finding that the reimbursement restrictions favored Blue Diamond over other participants in the marketing order.

Additional challenges came thereafter. The majority of cases originated in California, the home of the Ninth Circuit. The Third Circuit in *Frame* and the Ninth in *Cal Almond* had given conflicting decisions on similar programs. There was no clear indication of what precedent, if any, should apply. The United States Supreme Court would have to get involved.

The case that eventually reached the Court, *Wileman Bros & Elliot, Inc. v. Espy*, involved California nectarines, peaches, and plums marketed under the California Tree Fruit Agreement. Although the tree-fruit marketing order did not allow for reimbursement of advertising expenditures, many of the arguments heard in *Cal Almond* also arose here, including the charge that certain generic advertisements favored products distributed by particular handlers. The Court ultimately decided that because the plaintiffs had voluntarily participated

United States v. Frame

L. Robert Frame, who raised and auctioned cattle in Pennsylvania, refused to pay assessments mandated under the amended Beef Promotion and Research Act of 1976. Frame argued that the program violated his First Amendment rights by compelling him to associate with his competitors and pay for advertising when he would prefer to remain silent. In 1988 the Third Circuit Court of Appeals (885 F.2d. 1119) set forth the following framework to scrutinize the Act:

[W]e will sustain the constitutionality of the Beef Promotion Act only if the government can demonstrate that the Act was adopted to serve compelling state interests, that are ideologically neutral, and that cannot be achieved through means significantly less restrictive of free speech or associational freedoms. (J. Scirica (p. 1134))

The Court concluded that the 1976 Act met these tests.

1969: Abood v. Detroit Board of Education

1960 *1970*

in the regulated market, they were obliged to participate in the generic promotion program.

Here We Go Again?

The *Wileman* decision appeared to have put an end to further litigation when the Sixth Circuit issued its 1999 ruling in *United Foods, Inc. vs. United States* (see the sidebar on p. 22).

The ruling affects only a small industry, and its scope at present is limited to stand-alone promotion programs (that is, programs that are not a part of a broader regulatory scheme) in the Sixth Circuit. However, the decision carries ominous implications for commodity advertising programs, since it appears to rule out the legitimacy of stand-alone promotion programs in the absence of a "broad regulatory environment."

If the logic of the *United Foods* ruling is adopted by other courts, stand-alone promotion programs are threatened. Indeed, most state-authorized orders and commissions exist primarily to fund collective research and promotion. Lee et al. (1996) identified 36 such state-authorized promotion programs for California alone.

Promotion funded by orders with broad regulatory powers is not necessarily immune either. There appears to be limited understanding on the Sixth Circuit's (and, perhaps also the Supreme Court's) part concerning the degree of regulation at issue in *Wileman* under the tree-fruit agreement. Although the Agreement does authorize grade, size, and container regulations, it does not authorize direct volume controls (Lee et al. 1996). Neither does it result in uniform prices, as implied by the Sixth Circuit. If advertising conducted under a stand-alone program is unconstitutional, but the extent of regulation in California tree fruits is sufficient to justify collective advertising, where along the continuum of regulatory intervention should the line be drawn? The Sixth Circuit's opinion appears to invite more litigation.

Commodities and Brands: What's Next?

Where does agriculture go from here? Studies commissioned to assess the impacts of generic advertising

Cal Almond v. United States Department of Agriculture

In 1984, Saulsbury Orchards refused to pay its advertising assessments. Most of Saulsbury's sales were to cereal manufacturers. Saulsbury helped fund advertisements for some of the almond-containing cereals, and provided almond-related advertising for a chain of mini-markets that carried Saulsbury almonds. The Almond Board denied Saulsbury reimbursement for its advertising expenditures because Board regulations required consumer products to contain at least fifty percent almonds in order for the advertising to be eligible for reimbursement. The cereals did not meet this standard.

The Board denied the mini-market claim because Saulsbury did not operate the retail outlets. Indeed, among almond handlers only Blue Diamond operated retail outlets. The Board denied another handler, Cal Almond, Inc., credit for its contributions to advertising for ice cream containing its almonds. Blue Diamond, however, was able to recoup most of its advertising expenditures under Board guidelines.

In 1987, Cal Almond joined Saulsbury in challenging the Order based on arguments similar to those raised in *Frame*. In 1993 the Ninth Circuit Court of Appeals used the three-pronged *Central Hudson* test to reverse a lower court's ruling in favor of the order (14 F.3d 429). The Circuit Court agreed that the Almond Order's enhancement of demand for almonds was a substantial government interest. However, it balked over prongs two and three.

Regarding the second prong, the Court observed that neither USDA nor the handlers could provide evidence that the Board's advertising had any effect on almond demand and, thus, could not show that the generic promotion "directly advanced" the government's interest. On the final prong, the court held that the regulations were more extensive than necessary to further the government's interest in selling almonds, chiding the USDA for allowing reimbursement restrictions that appeared to have been put into place primarily to benefit Blue Diamond.

***1973:* Central Hudson Gas & Electric v. Public Service Commission of New York**

1976:* Beef Promotion & Research Act *(United States v. Frame)

1980

on the demand for particular commodities have found in most cases that generic advertising does increase demand. Nonetheless, some growers and handlers feel very strongly that they have been harmed by the orders that support this advertising.

Failure to address their concerns may mean that these growers will work through their commodity boards to jettison promotion programs that, on balance, have served farmers well. Indeed, acrimony within an industry can threaten the existence of an order. In 1994 the Secretary of Agriculture terminated both the navel and Valencia orange marketing order and the lemon marketing order due to squabbling and litigation among participants over alleged filing of false claims.

Advertising campaigns that promote a particular type or variety of product may harm producers and marketers of competing varieties. In *Cal Almond* the Ninth Circuit saw that Almond Board regulations benefited Blue Diamond's growers over other order participants. The heart of the plaintiffs' grievance in *Wileman* concerned differentiated products and the claim that generic advertising sent consumers a message that all California nectarines, for example, were of the same quality.

Now, the plaintiff in *United Foods* has raised successfully a product differentiation argument. Yet the issue of product differentiation is almost never addressed in discussions of *Wileman* or related cases, and among the dozens of generic promotion studies that have emerged since *Wileman*, none have considered differential effects based on degree of product differentiation.

A generic advertising program's underlying premise of homogeneous farm products is nowadays question-

Wileman Bros. & Elliot, Inc. v. Espy

The plaintiffs in *Wileman* argued that certain assessment-funded necatarine ads advanced the message that "red is better." They cited an assessment-funded promotional chart that listed a proprietary variety of nectarine—the "Red Jim"—owned by a member of the Nectarine Administrative Committee (58 F.3d 1377).

The handlers also complained that generic advertisements suggested that "all California fruit is the same," hurting attempts at product differentiation. Their own advertising was intended to convince consumers that their fruit was different from their competitors', yet they were being forced to "pay into a fund that advertises that all peaches and plums are the same" (Los Angeles *Times*, November 29, 1996.)

In hearing *Wileman*, the Ninth Circuit Court again applied the three-pronged test of *Central Hudson.* As in *Cal Almond*, the Ninth Circuit ruled that the tree-fruit agreement failed the second and third tests. However, in a 5-4 ruling, the Supreme Court (521 U.S. 457) used two main findings to reverse the Ninth Circuit. First, the court ruled that the handler's disagreement with some advertising content had no bearing on the validity of the entire generic program. Second, the court ruled that the Ninth Circuit had erred in using *Central Hudson* to test the constitutionality of the program.

Writing for the Court, Justice Stevens stressed the statutory context within which the generic promotion program had arisen and that the generic campaigns had to be viewed in light of the regulatory scheme that Congress had put forward.

California nectarines and peaches are marketed pursuant to detailed marketing orders that have displaced many aspects of independent business activity that characterize other portions of the economy in which competition is fully protected by the antitrust laws. The business entities that are compelled to fund the generic advertising at issue in this litigation do so as a part of a broader collective enterprise in which their freedom to act independently is already constrained by the regulatory scheme. (521 U.S. 468-469)

Congress had made a regulatory decision allowing certain commodities to be marketed jointly. With an *Abood* test, the Supreme Court ruled that the government's legislative action alone was enough to satisfy the necessity of the program. Whether individual growers and handlers were hurt was not a matter for the Court, because those growers had chosen to operate in a regulated environment.

1984: **Saulsbury Orchard refuses to pay assessment to Almond Board *(Cal Almond v. USDA)***

able, as more and more growers and handlers attempt to persuade consumers that their products really are different from everyone else's.

Timing of advertisements is also a crucial factor for many commodities. Producers and handlers have made strategic investments, such as choosing varieties and growing locations, to be able to supply products during particular market windows. For example, the most popular varieties of California table grapes, Thompson Seedless and Flame, are available June through November. Other California varieties are available much later in the season—September through February. Advertising by the California Table Grape Commission (CTGC) demonstrates awareness of this issue, as expenditures appear to vary with the time of year, in hopes of targeting key market windows. A recent evaluation of the CTGC's promotion program by Alston et al. (1997) reveals it to be very successful, but their study made no separate analysis of impacts by variety or market window.

This discussion should provide some insight into the issues underlying the recent legal attack on marketing orders. In addition, the economic issues underlying the complaints should not be brushed aside regardless of particular court decisions. Marketing orders were established to raise the tide for the entire industry. Unless commodity boards check to see that all boats are floating, they may eventually find themselves scuttled.

United Foods, Inc. v. United States

United, a Tennessee food processor, challenged the 1990 Mushroom Act on compelled commercial speech grounds and argued that the mushroom industry differed from the tree fruit industry sufficiently to make *Wileman* inapplicable. United seized on Justice Stevens' language characterizing the tree fruit advertising as part of a broader regulatory scheme for the industry. Such regulation, United argued, was absent for mushrooms, since the Mushroom Act was a "stand-alone" piece of legislation similar to the Beef Promotion Act at issue in *Frame*.

United argued that one outcome of a broad regulatory environment enacted under some orders is to reduce product differentiation through such things as standardized containers and grades, thereby justifying collective advertising. Without this regulation, mushroom producers and handlers could "freely differentiate their products and stimulate demand through competitive advertising."

Despite approving of Justice Souter's dissent in *Wileman*, a three-judge panel of the Sixth Circuit Court did not rely on his argument that the *Central Hudson* tests should have been applied in *Wileman* rather than the majority's application of *Abood*. Rather, the panel simply dismissed advertising programs that were not part of a broad regulatory scheme.

This point is important because under Souter's interpretation, industry could work to design programs that would pass constitutional muster. *United Foods* appears to simply slam the door on stand-alone promotion programs.

In March 2000, the court denied a government petition for re-hearing before the full Sixth Circuit. The ruling thus created an immediate conflict within the circuits because the *Frame* decision by the Third Circuit also pertained to a stand-alone program, and the Supreme Court declined to hear *Frame's* appeal, making the Third Circuit's ruling all the more curious. Not surprisingly, the U.S. Solicitor General has elected to appeal the case to the Supreme Court, which has agreed to hear it during the current term.

For More Information

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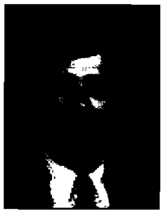
Lee, H., J.M. Alston, H.F. Carman, and W. Sutton. "Mandated Marketing Programs for California Commodities," Giannini Foundation Information Series No. 96-1, 1996.



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1990: **Mushroom Act *(United Foods v. United States)***

1996: Wileman Bros. & Elliot, Inc. v. Espy

1990 ***2000*** ***2001***