IN THE MATTER OF THE
NATURAL PRODUCTS MARKETING (BC) ACT
AND AN APPEAL FROM A DECISION CONCERNING EQUALIZATION OF HOG PRICES

BETWEEN

JAN BINNENDYK, RON BOES, AND JERRY GELDERMAN

APPELLANTS

AND

BRITISH COLUMBIA HOG MARKETING COMMISSION

RESPONDENT

DECISION

APPEARANCES:

For the British Columbia Farm Industry Review Board:	Sandi Ulmi, Vice Chair, Panel Chair Ron Kilmury, Chair, Panel Member Derek Janzen, Panel Member
For the Appellants:	John Durham, Agent
For the Respondent:	George Leroux, Chair
Dates of Hearing	January 10-12, 2011
Place of Hearing	Abbotsford, BC

INTRODUCTION

1. The appellants, Jan Binnendyk, Ron Boes and Jerry Gelderman, are all hog producers in the Fraser Valley region of BC.

2. There are two major hog processors in BC – Britco Pork Incorporated (Britco) located in Langley, and Johnston Packers Ltd. (Johnston's) in Chilliwack. In September 2010, at the time of the British Columbia Hog Marketing Commission's (Commission) decision under appeal, all three appellants were shipping their hogs to Britco.

3. There has been a difference in the price paid to producers shipping their hogs to Britco and Johnston's for some time. To address this perceived inequity, for several years, the Commission carried out a "pooling"[1] or "equalization" program that "topped" up the payment to Britco shippers so they received a similar price for their hogs to that of the Johnston's producers.

4. There has been controversy within the industry about this equalization program for many years resulting in a supervisory review by the BC Farm Industry Review Board (BCFIRB). On November 14, 2007 BCFIRB issued the *Supervisory Review of BC Hog Marketing Commission Price Equalization Program*. This review, among other things, directed the Commission to freeze the price equalization payments until it undertook further consultation with the industry and made a recommendation regarding the future of the program to BCFIRB. BCFIRB also directed that numerous governance issues in the administration of the program be addressed.

5. After significant consultation, both within and outside the industry and an industry-wide vote on the matter, the Commission voted on September 29, 2010 not to proceed with equalization. This appeal stems from that decision.

6. The appeal was held in Abbotsford on January 10-12, 2011.

ISSUE

Did the BC Hog Marketing Commission err in its September 29, 2010 decision not to proceed with an equalization program?

BACKGROUND

7. There is considerable history to the equalization program that precipitated this appeal. It has been contentious in the industry for some time and has caused strong divisions between producers, with some favouring the program and some strongly

[1] Equalization is not the same as price pooling under s. 11(1)(l) of the *Natural Products Marketing (BC) Act* – a power which the Commission does not have. Rather, the Commission may equalize or adjust producer returns using levies in accordance with s. 11(o)(iv) of the *Act*.

against it. In order to place this appeal in context it is necessary to understand some of the past history and the situation as it exists today.

History of Price Equalization by the Commission

8. Price equalization has been carried out by the Commission throughout the 1980's, 1990's and early 2000's. The program was designed to address the difference in price paid to producers by the major processors of hogs in BC. Equalization was achieved through pooling returns with the Commission serving as a "single desk seller". These powers were reviewed by Government as recently as 2004, following the Core Review.

9. Equalization was stopped in May 2004 when the price differential between processors was minimal. By July 2004, the price differences again began to increase. In May 2005, the Commission reinstituted the price equalization program and began equalizing producers shipping to Britco in July 2005. Payments were made retroactive to July 2004.

10. Payments under the equalization program were made from June 2005 until November 20, 2007, when the program was discontinued based upon the directions given in BCFIRB's Supervisory Review of the program.

11. The Commission has not run an equalization program since it was suspended in November 2007.

BCFIRB's Involvement in Price Equalization in the BC Hog Industry

12. The findings of the supervisory review carried out by BCFIRB were released in a report titled *Supervisory Review of BC Hog Marketing Commission Price Equalization Program*[2] on November 14, 2007. The supervisory review examined the price equalization program operated by the Commission between January 1, 2004 and December 31, 2006. At the outset of this time frame, 16 producers shipping to Britco were issued payments to equalize their returns to the level similar to those being received by the 18 producers shipping to Johnston's. Many of the Britco shippers subsequently moved to a direct contract system with Britco and the Commission then excluded them from the equalization program. By November 2005 there were only three shippers remaining in the equalization program. They continued to receive equalization payments until sometime in 2007 and two producers received payments as late as August 2007.

13. In its review, BCFIRB found that while the Commission had the appropriate regulatory authority and made an acceptable decision in embarking on the equalization program, it fell short in the design and implementation of the program in the following respects:

[2] The complete report can be found on BCFIRB's website at
http://www.firb.gov.bc.ca/reports/hog/07_nov_14_hmc_equaln_supervisory_review_rprt.pdf

(1) By not making the program self-financing through a levy applicable to all producers;
(2) By enabling only one processor (Britco) to engage in direct contracting, without considering whether such a policy should extend to all processors, and in that context, considering the long-term implications of direct contracting on producer prices;
(3) By continuing to make equalization payments that resulted in the returns to ongoing equalization program participants being greater than those received by Britco direct producers after it had determined that Britco direct producers did not require equalization;
(4) By not requiring all producers to pay the levies that it had established in order to rebuild the Trust Fund; and
(5) By not paying outstanding equalization balances to producers who went out of business during the price equalization program.

14. Further, BCFIRB identified a number of issues regarding the Commission's governance and administration of the equalization program.

15. BCFIRB's November 2007 report issued a set of supervisory directions with respect to the equalization program. These included that payments under the program be immediately stopped, that administrative problems associated with the program such as balances owing to producers be addressed, and that, once these had been addressed, the Commission make recommendations as to whether equalization should continue. BCFIRB directed that if equalization was to continue, the governance issues related to the program would have to be addressed.

Commission's follow up to BCFIRB's Supervisory Review

16. From November 2007, until September 2008, the Commission consulted with the industry to respond to BCFIRB's directives. On September 8, 2008, the Commission made its final recommendations on the price equalization program to BCFIRB. The recommendations indicated that the Commission had ceased its price equalization program on November 20, 2007, and outlined how the Commission proposed to address a number of outstanding administrative and governance issues with respect to the equalization program.

17. BCFIRB replied to the Commission's final recommendations on November 28, 2008, noting that although the recommendations deviated from some of BCFIRB's past supervisory directions, BCFIRB was prepared to accept them because they offered a practical way forward for the Commission and the industry.

18. The Commission's final response did not provide a recommendation as to whether equalization should continue, but rather noted that this was an issue to be discussed with and decided by all producers going forward. The Commission continued to discuss with registered producers whether a new equalization program was desirable, holding meetings on the subject in September and November of 2008. At the November meeting, the chair presented a preliminary proposal for a four-year

declining equalization program (i.e. starting with 100% equalization in 2009, declining by 33.3% annually to no equalization in 2012). The proposal was further developed and presented to producers at a meeting on January 26, 2009. At that meeting, the Commission also specified that it would conduct a vote to determine producer support for the equalization proposal and reviewed the ballot question and submission procedures with producers.

Hog Commission Equalization Ballot

19. On January 29, 2009**,** the Commission conducted a vote on the equalization proposal of those registered producers who shipped to Britco or Johnston's in 2008, and continued to ship to one of those packers in January 2009. The ballot specified that equalization would proceed if 70% of the producers voting and representing 70%+ of the total average weekly shipments during the September 1 to November 29, 2008 period voted for the proposal.

20. The equalization vote had an 85% response rate, but failed to receive the required level of support in terms of number of producers or volume of production.

Correspondence with the Minister of Agriculture and Lands

21. In February 2010, a group of six BC hog producers wrote to the then Minister of Agriculture and Lands. The group, which included one Commission member, expressed a lack of faith in the Commission and in BCFIRB with respect to actions that the two boards had taken around equalization, and requested the Minister's immediate assistance. The producers met with the Minister on February 24, 2010.

22. On March 25, 2010, the Minister wrote to BCFIRB, and asked if BCFIRB would consider assisting the Commission in moving forward on the equalization issue. The Minister asked BCFIRB to consider directing the Commission to engage a third-party contractor to provide an analysis with respect to the future of equalization.

23. In response, BCFIRB wrote to the Commission on April 14, 2010, indicating that while BCFIRB had the authority to direct the Commission with respect to equalization, it was of the view that decisions on policy (including equalization) should be made by the Commission in the first instance with that decision being appealable to BCFIRB. BCFIRB also indicated that the Minister's suggestion of engaging a third-party contractor was one of the options that could be considered.

24. At its May 19, 2010 meeting the Commission decided to engage a third party to look at two main areas underpinning the debate around equalization including:

    (a) Regulated marketing approaches in other jurisdictions, how these have evolved over the past decade, the conditions under which equalization exists, and where it once existed but no longer does; and,

(b) Production cost differences for the different hog specifications utilized by BC's two main processors.

25. The contractors were specifically directed not to provide an opinion on equalization. It was agreed that the chair would issue a written position on equalization following receipt and review of the study. The Commission subsequently engaged the George Morris Centre to conduct the study.

George Morris Study

26. In September 2010, the George Morris Centre provided its final report on equalization to the Commission. The report detailed the movement in the prairie provinces from single desk to open marketing systems during the mid-late 1990s, and suggested that similar trends were underway in eastern provinces. It suggested that the Canadian hog industry was increasingly characterized and governed by:

(a) Direct negotiation between producers and individual processors to establish long-term supply and pricing arrangements;

(b) The establishment of integrated business structures where producers and processors are mutually invested…

27. The report concluded that the more rapidly provincial or regional hog industries are able to move toward either of these two alternatives, the more likely they will be able to achieve competitiveness over the long term. The report also provided data on the production costs associated with meeting the different hog specifications of BC's two main processors.

28. Following his review of the George Morris Centre report, the chair of the Commission released his written position on equalization for the BC industry on September 10, 2010. The chair concluded that equalization is not sound marketing policy in BC, setting out multiple reasons for his finding, most of which related to the increasingly global structure of the North American hog industry, the fact that single desk selling is no longer used in the Prairies and has been 'unwinding' in Eastern Canada, and the fact that equalization could work against both the ongoing differentiation strategies of BC processors and the value chain relationships that BC producers needed to develop with their processors in order to remain competitive. This position was circulated to producers along with the George Morris Centre report.

29. On September 29, 2010, the Commission met and considered the George Morris Centre report and the chair's written position. The Commission then voted not to implement equalization. This is the decision under appeal.

Current Market Conditions in the BC Hog Industry

30. The period from 2004 to the present has been an extended period of low market prices for hogs. This period has also experienced high feed input costs and an appreciating Canadian dollar that has negatively affected hog exports. The result is that producers have experienced significant losses, with those shipping to Britco suffering higher losses than producers shipping to Johnston's.

31. Canada's pork industry competes on a global basis. BC is a high cost region to produce hogs due to the fact that the majority of feed meals and grains must be brought in from other regions. In addition, land costs are high and economies of scale are not common, unlike other areas where there has been significant producer consolidation resulting in larger, more efficient farms.

32. The BC hog industry has been drastically reduced over the past few years, moving from around 300 hog producers to the situation today, where there are less than 30 producers shipping approximately 15% of the pork consumed in the province. The processing sector has shrunk from 6-8 plants down to the two left today – Britco and Johnston's.

33. Britco, a federally inspected plant, processes up to 7000 market hogs per week. Johnston's is provincially inspected and processes 1500-1700 market hogs per week. In addition, both plants process round hogs which are carcasses sold whole into the ethnic market and used for barbequing. In total, BC produces approximately 3000 market hogs per week. This shortage results in Britco sourcing 80% or more of its live production from Alberta. Producers shipping to Britco but wanting to ship elsewhere must either get Johnston's to purchase their hogs or ship out of the province. Presently, Johnston's does not have the capacity to process all of the BC production. At the time of this hearing, there are three BC producers shipping to Britco with the remaining shipping to Johnston's.

34. Britco and Johnston's have different marketing strategies and require different market hog carcass weights. Britco wants a 92 kg carcass weight, while Johnston's requires an 82.5 kg carcass. There are cost of production differences to produce the different hog sizes required by both processors. There is little consensus among producers as to the actual dollar value of this difference, but it is generally thought to be in the range of $15-$18 per hog.

35. Prices paid by Johnston's are higher than the prices reported by Agriculture and Agri-food Canada for any other province in Canada. Prices paid by Britco track closely to the prices paid by the processors in Alberta, Saskatchewan and Manitoba.

Legal Authority of the Hog Marketing Commission

36. The BC hog industry has been regulated under the *Natural Products Marketing (BC) Act* (the *NPMA*) and the *BC Hog Marketing Scheme* (the *Scheme*) since 1980. The Commission was delegated the authority to market all hogs in the province in 1983. Under section 6(1) of the *Scheme*, the Commission has the authority to "promote, control, and regulate any aspect of the marketing of the regulated product". Under section 6(2), of the *Scheme*, the Commission has the power to set or collect levies and equalize or adjust producer returns. It does not have the powers to set price or regulate production levels.

ARGUMENTS OF THE APPELLANTS

37. The appellants' central argument is one of fairness. They argue that there is a major difference in pricing between Johnston's and Britco and the only fair way to address this issue is through equalization of price. They state that there is a significant difference in the price paid per hog to producers shipping to the two plants. They argue that it is not fair that producers should receive different prices for their hogs and that this has created financial hardship on those shipping to Britco and a great deal of controversy in the industry.

38. On February 23, 2010 the appellants along with three other hog producers wrote to the then Minister of Agriculture and Lands to state their frustration with what they saw as unfair treatment. The letter said in part:

> …In the past five years, the **BCHMC has failed** in treating all producers equally. **FIRB has also failed** in their responsibility to step in and rectify the inequality that has been and is taking place in the industry. We have lost our confidence in both the commission and in BCFIRB for how they failed in their responsibility to treat all producers fairly and equally. (emphasis in original)

39. The appellants contend that the vote against equalization by producers was a foregone conclusion as most producers ship to Johnston's and are receiving the higher price and no longer want to support their fellow producers. They maintain that the industry should be working together for the good of all producers and that this is the role of the Commission and why it was put in place in the beginning.

40. Further, they argue that there has been equalization for 25 years and that producers have traditionally supported the program. The appellants also point out that equalization goes both ways and that in the past Britco has received more money than Johnston's shippers and if this was to happen again, Britco shippers would equalize Johnston's shippers.

41. Jake DeWit, gave evidence for the appellants. He produced hogs for approximately 25 years until retiring in October 2010, and was chair of the BC Pork Producers Association for about 10 years. He claims that "Britco held us ransom" and had a "take it or leave it" policy which made it difficult with only two processors where it

became a situation of who could get into the higher paying plant. He stated that all producers should be working together and should be paid the same price because the pigs are the same, but one is heavier. He further stated that he was frustrated with BCFIRB for not "putting the thing to bed" in 2008. "I struggle with the past", he said.

42. He maintains that BC is unique and different from the rest of Canada. He does not agree with the findings of the George Morris Centre report or that of (management consultants) Toma & Bouma who claim that equalization is not the way the hog industry is managed in other jurisdictions.

43. One appellant, Mr. Boes, has been hog farming since 1983 and a director of the Commission for the last 10-12 years. He would like to see the industry working together as one body. He maintains that since pooling has fallen apart he finds it much harder financially. Mr. Boes claims that while BCFIRB had some misunderstandings of the Commission in its 2007 Supervisory Review, it had sound recommendations and was aware of the need for equalization. His interpretation of the report is that BCFIRB wanted to clean up the program and make it better going forward.

44. Another appellant, Mr. Gelderman has been a hog producer since 1978, a director on the Commission from 1997 until 2009, and chair of the Commission for four years. He is one of three BC producers shipping to Britco. He states that the May 17, 2006 letter to BCFIRB explains the Commission's view on equalization. The letter states:

> The British Columbia Hog Marketing Commissions' [*sic*](BCHMC) role as a marketing board is to achieve a fair price of the regulated product for all producers in British Columbia as outlined in the National [*sic*] Products Marketing (BC) Act Regulations definition "marketing" includes producing, buying, selling, shipping for sale, offering for sale or storage, and in respect of a natural product includes its transportation in any manner by any person. We do this by equalizing the prices we receive from different processors, whether they are local, inter-provincial or to the United States. By doing this, it stops individual producers from fighting each other in an open market place. Any premiums or bonuses over and above the equalized base price is for the producers [*sic*] benefit and is not included in the equalization. We are not supply managed nor do we have the ability to set the price as in the National [*sic*] Product [*sic*] Marketing Act 11(k). This practice has worked well for all BC producers since the conception of the BC HMC. Equalization has been done throughout the entire history of the BCHNC [*sic*] except for the short period of May 14, 2004 through June 3, 2005.

45. He notes his frustration that it took two years to make the decision not to equalize and that the decision just kept getting postponed. He claims that he did not want to bring the Commission discussion on equalization to a vote as there were two directors on the Commission shipping to the lower paying plant, and one shipping to the higher paying processor, and if the chair had voted against equalization, the motion would have failed.

46. Mr. Gelderman further states that the directors on the Commission believed that a motion to equalize should have come from a producer shipping to Johnston's and that that didn't happen. He states that Britco is still punishing the industry for historical wrongs and he is paying the price for the industry.

47. He argues that the KPMG report found no irregularities in the equalization program and that while BCFIRB found problems with the management of the program, it had no problems with the program itself. Mr. Gelderman states that he believes that equalization equals fairness and that the Commission should work toward getting the best returns for all producers. He contends that equalization should be re-implemented and financed going forward through a five-cent levy on all producers.

48. Mr. Gelderman also argues that the George Morris Centre report did not follow the exact wording in the March 25, 2010 letter from the then Minister of Agriculture and Lands to BCFIRB. He contends that the words in the Minister's letter suggesting that the third party review "*would* have to consider the advisability, policy implications and risks of all possible options" and "an analysis of how to implement the option should also be provided" were not reflected in the April 14, 2010 letter to the chair of the Commission from BCFIRB. This letter stated, "a third-party contractor *could* be engaged to provide an analysis with respect to the future of equalization and agrees that this is one of the options that could be considered."

49. The third appellant, Mr.Binnendyk, states that their family farm, Excelsior, is one of the largest hog farms in BC with 1250 sows. Until recently, Excelsior has been shipping to Britco at the direction of the Commission and receiving $16-20 less per hog. On top of receiving less per hog at Britco, Excelsior pays $25,000-$30,000 per year to the Commission. Excelsior has recently begun shipping to Johnston's. Mr. Binnendyk says that they had to change their barns at considerable cost to go with the heavier hogs. The difficult financial time of the past few years has been very hard emotionally on his entire family and he feels that his family is carrying an extra debt load to help out other farmers.

50. As a remedy, the appellants want the equalization program reinstated. This program would need to "equalize the past and equalize going forward". They are looking to BCFIRB for assistance with developing a financial vehicle to help in accessing funds to be repaid with a dedicated levy that could be used for other things when it has fulfilled its purpose.

ARGUMENT OF THE RESPONDENT

51. George Leroux, chair of the Commission as of 2008, argues that equalization is not sound marketing policy for several reasons.

52. Firstly, he points to the facts that the Commission has not successfully negotiated contracts with the processors since 2003; that all contract-related payments

including round hog orders and related management expired by 2005; that since 2004 there have been different levies for different people; and finally, that in the past, the Commission deliberately kept Johnston's in the dark and uninformed of what it was doing with Britco. Because of this lack of clear policy and poor management within the Commission, Mr. Leroux argues that the Commission has lost credibility with the industry and "abandoned the future opportunity to equalize".

53. Secondly, Mr. Leroux argues that equalization is incompatible with present trends in the industry, as has been demonstrated by the reports of the George Morris Centre and Toma & Bouma management consultants. He agrees with them that the only option for BC is for higher valued products that can recover higher costs and argues that BC producers and processors are already doing this without regulation. In his opinion, equalization is completely at odds with the requirements of the market place.

54. Thirdly, he argues that equalization is not supported by the majority of producers or either of BC's primary processors.

55. Kevin Grier is a senior market analyst with the George Morris Centre, an independent organization that conducts economic research into the agricultural and food industries. He has worked on over 40 projects on hogs since joining the Centre in 1996 and states that approximately half of his work is to do with hogs. He was the major author of the third party review prepared for the Commission in September 2010. The purpose of the project was to provide a review of the issues surrounding the practice of price equalization for hogs in Canada together with a cost of production analysis for different sizes of market hogs.

56. In summary of the report, Mr. Grier states that:

- hog and pork prices are determined globally and the hogs will flow to the higher prices;
- there has been dramatic rationalization of herds and packing plants in Canada in the last five years;
- the largest plants have shown to be more competitive and have the lowest costs and have survived;
- small and mid-sized plants are going out of business;
- small packers deal with small grocers and cannot get more money as small grocers are competing with large grocers, although unique characteristics may add some value;
- large packers deal with large grocers;
- every packer has unique contracting practices but in Canada 85% of hogs are contracted.

57. He claims that hog pricing in Canada is determined by the packer's ability to compete with their counterparts in the US and Canada and while there are a variety

of contracts and formulas, the price is ultimately based on the US market, the exchange rate and the “basis” or local spread.

58. Mr. Grier notes that a processor may pay more to ensure that his local supply remains strong, but that pork is not significantly different from one producer to another. Processors do not ordinarily pay more than others, making the higher paying Johnston’s an unusual situation. On the retail side, pork is extraordinarily cost competitive and price sensitive and the retailers do not care where they get their pork from, merely the price they must pay for it.

59. When comparing the costs of growing a 92 kg hog with that of an 82.5 kg hog, Mr. Grier states that the heavier hog has a higher cost of production per pig, but a lower cost per kilogram of carcass weight. The additional cost is due to the extra feed used and the greater barn space required.

60. Mr. Grier states that Quebec is the only province that equalizes prices between processors through pooling; however the important difference in Quebec is that the government subsidizes producers and funds the difference between the price producers receive from processors and their cost of production including a margin. He described this as a social contract with producers. No such subsidy exists in BC.

61. Jerry Bouma, B.Sc., M.Sc., a partner in Toma & Bouma Management Consultants, a specialized in agri-food management firm providing strategic planning and market and business analysis testified on behalf of the Commission. He has worked in the hog industry monitoring trends and doing market research for over 30 years. Mr. Bouma notes the trends to integration in the US hog industry where there is movement toward a single bottom line where producers and processors work together using cost centres and what is left over at the end of the day gets shared between them. He states that some producers and processors in Alberta are working to create this interdependent kind of model where producers are shareholders in the processing plants and share in revenues rather than being paid for product. The focus in this type of business arrangement becomes what the business should be, not disputes over what should be paid for raw material. Linkages and coordinated production are now cornerstones of the Canadian industry.

62. Mr. Bouma states that the ideal conditions for regulated marketing existed 30-35 years ago when there were a large number of producers and no price transparency. At that time marketing boards brought focus and order into the system. However, everything has now changed beginning with the decision in Manitoba in 1996 to move away from single desk selling. The conditions under which equalization systems were formed no longer exist. He further contends that the more a provincial board attempts to control the marketing options facing producers, the more rapidly the system begins to implode.

63. In August 2008, Toma & Bouma produced an *Opportunities Assessment Phase 1 Report – Towards a Strategic Plan for the BC Pork Industry* to determine whether

there are unique market opportunities within BC and what opportunities and constraints face the BC pork industry in pursuit of those opportunities. The report concluded that there is a real and growing interest in BC in locally based products but that this market is small and would need to be developed carefully. There was recognition that price is a major driver and that the market is very competitive. Further, it was noted that the BC pork industry, which, according to Toma and Bouma, supplies approximately 15% of provincial demand, has little or no image within BC.

64. Toma & Bouma also developed confidential strategic plans with both BC processors and a final *Strategic Plan for the B.C. Pork Industry* that was submitted to the BC Pork Producers Association in March 2009. Mr. Bouma noted that the two BC processors operate totally differently, with Johnston's priding itself on service, with its focus being small, local groceries and delicatessens. Britco brings in most of its hogs from Alberta for processing and works mainly with large retailers and chain stores. Presently they compete with each other only to a limited extent.

65. Mr. Bouma states that there is a need for the industry to understand both models and if the Commission tries to force them to do business in a certain way, they will simply do business elsewhere. He states that both businesses are successful in their own way and the fact that two packers have survived in BC is a real testimony to the good work that they both do. In Bouma's opinion, "if equalization is brought in, one or both processors will leave."

66. Rick Thiessen, a poultry and hog farmer who started shipping hogs four years ago and was a member of the Hog Commission from 2007 until 2010, gave evidence of his experience of shipping to Johnston's and then moving to Britco. Thiessen ships half of his production as round hogs and half as market hogs. He states that if he combines the negotiable round hog price with the market hog price, his net bottom line is not significantly different from what it was at Johnston's. Mr. Thiessen testifies that in his experience, the net difference between Johnston's and Britco of $18 as argued by the appellants, is overstated.

67. Mr. Thiessen states that he is not a proponent of equalization because:
   - the Commission has no influence or impact on where his hogs are being shipped and could not have helped him to stay at Johnston's. He is free to find another home or get out of the industry; and
   - the Commission no longer negotiates price on behalf of producers.

68. Mr. Thiessen asks: "How can you equalize business opportunities?" He goes on to ask, 'If the Commission is not negotiating price or directing hogs, how can you equalize?" In his opinion, if the Commission is not negotiating price or directing hogs, he does not see a place for it.

69. Ivan TenBos has been working at Johnston's, a small family owned business, since he was 17 years old and is now the Plant Manager. He states that Johnston's butchers approximately 1700 market hogs and 500 round hogs per week and also processes beef and lamb.

70. Mr. TenBos states that he feels the Commission deceived him in price negotiations in the early 2000's. He understood that Johnston's was paying the same as Britco, when in fact it was paying substantially more. He also states that the Commission did not tell him about the equalization that was taking place with the Britco producers and he never had any discussions with the Commission on the topic. Further, Johnston's was not notified or aware when the Commission allowed Britco to pay producers directly. As a result, he states that he lost confidence in the Commission directors of that time.

71. Mr. TenBos notes that Johnston's has always opposed equalization as it felt that equalization was in essence, subsidizing its competitor. He states that if equalization comes in, he would have to consider lowering his prices and Britco could possibly do the same. Regarding the higher price Johnston's pays its producers, Mr. TenBos states that Johnston's wants to be in business for the long term and that it values its shippers and customers. Even though prices have been poor and times difficult, Johnston's has continued to pay a higher price out of loyalty to its producers. He further states that the logical thing for Johnston's to do would be to reduce its price to be equal to Britco, but "morally we couldn't do that". Mr. TenBos argues that with equalization there is no incentive for producers to do anything to improve the quality of their product, as they would get the same price in the end in any case. It is his opinion that the industry must look forward instead of looking back.

DECISION

72. The panel has carefully considered all of the evidence and submissions provided during this hearing, even though we do not intend to refer to it all in the course of this decision. In light of our review, the panel has not been convinced that equalization is appropriate or the best choice for the BC hog industry going forward. We make this finding for several reasons.

73. The appellants presented considerable evidence on numerous topics such as the history of equalization and how it worked in the past, records of the investment fund and how payments were made from it, how and when contracts were negotiated between the Commission and processors, how the appellants had felt pressured by the chair of the Commission, and more. While the panel considered this evidence, we do not find it particularly instructive or helpful to the issue under appeal.

74. The appellants put forward three main arguments why equalization should occur. They argue that every producer should be paid the same amount per kg for a hog

regardless of which plant it is shipped to, as a "hog is a hog" and the hogs shipped to both plants are the same hogs, except for weight. Secondly, they argue that hog production in BC is different from the rest of Canada and while equalization may not be appropriate for the majority of Canadian production, it can and should be used here. Their third argument is that equalization is the only fair way to proceed and that it is the job of the Commission to be fair to all producers. We will look at each of these arguments in turn.

"A hog is a hog"

75. In the panel's view, the argument that all hogs are equal is flawed. We do not accept that the hogs required by the two processors have the same net cost of production per kg. There is considerable controversy regarding the cost of raising hogs to the different weights required by Britco and Johnston's. The George Morris *Equalization Review* found, and we accept, that the heavier shipping weight brings with it a higher cost per pig, but a lower cost per kilogram of carcass weight – thus affecting the net return. We also accept the evidence of Mr. Thiessen, that based on his experience of shipping hogs to both processors, the appellants are overstating the net price difference paid between Johnston's and Britco.

76. Regardless of the difference in cost to raise different sized hogs, the two processors do require different hogs and have different markets and pay different prices. We see no reason why processors should be forced, through equalization, to pay the same amount for differentiated products; nor do we think that would be fair, sustainable, or sound marketing policy. This argument would require the panel to accept that producers have little onus to adapt their operations to meet opportunities as they exist in the market place, both locally and globally. We cannot do that.

77. The appellants argue strongly that that the mission of the Commission is to negotiate the best price for **all** producers. In their opinion, this equates to equalization where all producers receive the same price. The panel does not accept this argument. In our view, the appellants are comparing themselves to those at Johnston's and feeling "hard done by" as they feel they receive less. They are not looking at the global picture, nor do they recognize that Johnston's is paying a loyalty premium. The appellants simply want to be paid the Johnston's price, not the Britco price per kg for their hogs. They are failing to recognize both the cost of production and market realities of producing different sized hogs as well as the fact that the prices paid by both Britco and Johnston's are among the highest in Canada.

78. The panel also does not accept the argument of the appellants that equalization is part of "working together as an industry". Working together as an industry does not mean, in our view, that everyone must be paid the same for their hogs. Equal payment does not recognize the differences in the industry such as the effort that Johnston's has put into developing relationships with its producers. In our view, Johnston's has been working to develop a "value chain" approach where it works with its producers to get the quality of product it needs, and with its customers to

deliver what they demand. Britco has a different purchasing and marketing strategy that involves little relationship building with its BC producers who supply less than 20% of its processing needs.

79. We agree with the point made by Mr. Bouma that while both processors are operating under different models, they are both successful as they are still in business. We also accept that there is a possibility, as he states, that: "if equalization is brought in, one or both processors will leave." We do not believe that possible outcome is in the best interest of BC's hog industry.

80. The panel heard from the appellants and their witnesses a great deal of the history of the equalization program and a "wish for the past". We recognize that change is difficult, especially in times of severe financial hardship such as the hog industry has experienced over the past several years. However, as demonstrated by the George Morris *Equalization Review*, the industry both in Canada and worldwide has, and continues to radically restructure. Businesses must change and adapt. Just because equalization was successful for a lengthy period in the past does not mean that it should continue without serious consideration of whether it serves the realities of today's world. Companies must be competitive, respond quickly to market demands, and be willing to look at new ways of doing business. It is time to look to the future, not to the past.

BC is unique

81. The appellants argue that while equalization may not be appropriate in other places, BC is unique with only two processors and very few producers. Equalization has worked here in the past and should continue to be the way the BC hog business is managed.

82. The panel does not agree. We accept the evidence of Mr. Bouma that equalization was beneficial many years ago when there were a large number of small-scale producers and many buyers with little information available to them. Across Canada, including in BC, this has changed to a situation of larger farms with a few large processing plants and pricing information readily available to both processors and producers, negating the need for single desk selling and equalization of payment. The fact that no other province continues to equalize payments, except Quebec where the government offers subsidies, suggests that the BC hog industry would fail to recognize the competitive realities in Canada, and globally, and would be taking a step backwards to implement such a program.

83. According to Toma & Bouma's research, BC produces approximately 15% of the pork consumed within the province. The rest is imported and price competitiveness is a major factor at the retail level where retailers source product nationally and even internationally. The Commission has no regulatory authority to control production or importation of pork into the province, or the authority to regulate pricing. The BC hog industry cannot avoid this reality. Without these authorities

the panel questions the viability of an equalization program over the longer term. As Mr. Bouma states: "you cannot out run your competition".

84. To this end, we further note the findings in the *Equalization Review* that the Canadian pork industry is increasingly governed by mutual interdependence and the need to satisfy the long-term financial objectives of both processors and producers. This is being accomplished through direct negotiation between producers and individual processors to establish long-term supply and pricing arrangements and the establishment of integrated business structures. We agree with Mr. Grier that "the more rapidly provincial or regional hog industries are able to move toward either of these two alternatives, the more likely they will be able to achieve competitiveness over the long term." Johnston's has consistently done this by working with producers and building relationships with them to ensure its long-term supply. In our view, equalization would have a negative effect on the development of these individual producer/processor relationships. We do not see how this could stimulate innovation or competitiveness in the BC hog industry.

Fairness

a) Fairness of Equalization

85. The panel turns now to the argument of fairness. While we understand the appellants' position, in our opinion, their view that receiving less for their hogs is unfair is more perception than reality. We fail to see how equalization is fair either to individual producers or to the industry as a whole when it has been rejected by the majority of both. Further, we do not see that fairness requires that all producers be treated equally on price when they are producing hogs to meet the specifications of their processing plants whose customers have different market requirements. As we have already noted, a "hog is not just a hog".

86. We accept Johnston's argument that it considers equalization unfair. As a processor it would be, in effect, subsidizing its competitor Britco and allowing Britco to continue paying lower prices. We understand why Johnston's would consider lowering the price it pays its producers if equalization were to occur and do not think that this would be a fair outcome to the industry at large. Johnston's has made a significant effort to develop good relationships with its producers and has paid higher prices to maintain these relationships and support its producers when the industry was suffering. We see no reason to jeopardize that relationship, nor do we think it would be fair either to Johnston's or to the producers shipping to them to do so.

87. The evidence given at the hearing indicates that there are only three BC producers shipping to Britco, one of whom testified in support of equalization, one of whom testified against equalization, and the other who did not appear. This leads us to conclude that there is, at most, two producers shipping to Britco who support equalization. In this case, to make regulation which benefits so few producers to the

possible detriment of others and the processing sector, is in our view, not fair, nor is it good regulatory policy.

(b) Fairness of the Process

88. The appellants argue that the process around the equalization decision was unfair for several reasons: it took too long; the industry-wide vote was a foregone conclusion because most producers ship to the higher paying Johnston's, and therefore were unlikely to vote for equalization; and the fact that they were afraid to bring equalization to a vote in case the chair voted and equalization would be turned down.

89. The panel can find no fault with the process undertaken by the Commission. We note that before the vote on equalization was held, the Commission held considerable industry consultation and many meetings held over a lengthy time period. In addition, to gain further insight into the issue, an independent third party was hired to conduct a review of equalization across Canada and a price analysis of the cost of production for different sizes of market hogs. Fulsome consultation takes time.

90. While the appellants complain about the length of time it took to come to the decision not to equalize, we note that at no time did they attempt to bring the issue to a vote at the Commission when two of them were members of the board. Both acknowledged that they could have done so. Refusing to bring the issue to a vote because of a fear that it will be democratically defeated is no grounds for complaint.

91. The panel also finds that the vote taken by 85% of BC hog producers that rejected equalization was fair and deserves serious consideration. The appellants admit that the process for the vote, including the threshold of 70% of producers representing 70%+ of the production was open and transparent. While it can be argued that the majority of producers are receiving the higher price and therefore have no incentive to vote for equalization, we accept that the process and protocol for this vote was discussed and agreed to by the Commission members and accepted as valid at the time. To not give considerable weight to this vote under these circumstances would, in our view, be unfair to all producers.

92. From our perspective, the chair of the Commission allowed the equalization issue thorough discussion in the industry and a generous amount of time for all opinions to be heard before a vote on the issue was taken. We accept that the Commission carried out a fair process before making the decision not to equalize.

93. In our view, it is time to let go of the battle over equalization and start working toward a new reality. Equalization has been a divisive force in the BC hog industry now for many years. It is time to accept that equalization is no longer compatible with the competitive and production realities of today's Canadian hog industry. It is

not a stimulus for the innovation and new business models that are necessary for the BC hog industry to be competitive in a small, specialized local market or on a larger basis. Both processors and their producers must work together, with their own individual marketing plans, to maximize their success.

Other Considerations

94. Finally, we note that many parties raised the issue of the need for the Commission and its relevance given the market realities of today. Several people asked that if the Commission does not negotiate price or direct hogs, what is its function? This issue goes beyond the scope of this appeal. However, the panel would observe that the hog industry has long been advised to involve itself in critical strategic planning to determine where it is going and what tools it requires to get there. We would anticipate that this strategic planning would involve a consideration of the role of the Commission, whether it has is a valid role, how the Commission should be structured and what constitutes an equitable voting mechanism. These questions must be considered by the industry to determine the future of the Commission. In our opinion, these matters should be dealt with as soon as possible to allow the industry to move forward.

ORDER

The appeal is dismissed.

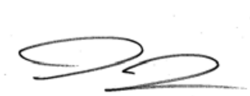
There will be no order as to costs.

Dated at Victoria, British Columbia this 1st day of March, 2011.

BRITISH COLUMBIA FARM INDUSTRY REVIEW BOARD
Per:

Sandi Ulmi, Vice Chair, Panel Chair

Ron Kilmury, Chair, Panel Member



Derek Janzen, Panel Member