

June 19, 2020

File No.: 580206-2

Sent Via E-mail

British Columbia Farm Industry Review Board
780 Blanshard Street
Victoria BC V8W 2H1

Attention: Kirsten Pedersen

Re: BCFIRB Supervisory Review – Interim Pricing Submissions

1. We write on behalf of the Primary Poultry Processors Association of British Columbia (the “**PPPABC**”) in response to the June 8, 2020 letter of the British Columbia Farm Industry Review Board (the “**BCFIRB**”).
2. The BCFIRB has asked for submissions on the following questions:
 - (a) Are one or more of the pricing structures in place currently resulting in industry instability?
 - (b) If current pricing structures are resulting in industry instability, what interim changes are necessary to create stability?
3. To answer the first question, the PPPABC believes that the two main pricing structures, the British Columbia live price formula and the linkage agreement, are causing industry instability.
4. The structure of the current live price formula results in a British Columbia live price that is unpredictable and uncompetitive, as it provides an avenue for stakeholders to pass on costs and margin increases onto processors without regard for the broader industry.
5. The decision of the British Columbia Broiler Hatching Egg Commission (the “**Commission**”) to step away from the linkage agreement and promote its own cost of production formula has added a new level of complexity to industry pricing. While the Commission’s maneuvers have benefitted hatching egg producers, it has not presented a viable solution to provide margin increases for hatcheries within the linkage agreement. The Commission’s actions have perpetuated the mindset that every stakeholder can pass along their own costs through to the processors.
6. On the second question, the BCFIRB should take the following interim measures to create stability pending a long-term pricing solution:

(1) Rescind the Commission's unilateral changes to the linkage agreement in the Commission's November 27, 2019 decision and Amending Order 26. This action by the Commission was designed to compensate hatching egg producers for premiums being received by broiler growers, even though those premiums no longer exist.

(2) Order that there be no further changes to the current live price formula or the factors within the formula during the supervisory review (subject to an appropriate safety valve). The PPPABC does not support the current formula but believes that temporarily locking the factors down will bring interim price stability.

(3) Order that any future reduction of the Ontario efficiency adjustments flow directly to British Columbia processors and hatcheries. Processors and hatcheries are the two industry participants who have largely paid for the efficiency adjustments by way of increased price differentials with Ontario.

(4) Implement a moratorium on growers moving amongst processors to prevent the re-introduction of loyalty premiums that de-stabilize the industry.

7. By taking these actions, BCFIRB will be levelling the playing field for all stakeholders and providing motivation for the parties to negotiate a long-term pricing agreement.
8. The supervisory panel must also consider the recent impacts of COVID-19. In their April 30, 2020 meeting, the BCFIRB, the Commission, and the British Columbia Chicken Marketing Board (the "**Chicken Board**") recognized that processors face increased costs due to the pandemic. Processors are absorbing increased costs from slower line speeds, wage premiums, increased overtime, and heightened occupational health and safety requirements. WorkSafeBC has visited most British Columbia poultry plants and it is clear that most of these increased costs will become permanent.

I. Pricing structures resulting in industry instability

A. Live price formula

(1) Background of current live price formula

9. While much can be said about the current pricing formula, the main issue is the instability inherent in the components of the live price formula. In particular, the formula provides each sector the opportunity to increase their margins or pass on their costs, which ultimately get passed along to processors, without an overall regard for the sustainability and competitiveness of the broader British Columbia chicken industry.
10. As the panel knows, prior to 2017, the British Columbia chicken industry set the live price of chicken based on a fixed differential over the Ontario live price. The BCFIRB mandated pricing model in 2010 used a weighted average of Ontario and Prairie live prices, plus a fixed differential. Prices were predictable, and industry stakeholders could focus on their businesses and broader industry issues, rather than pricing disputes. Between 2010 and 2015, the live price differential

between British Columbia and Ontario was no more than \$0.0571 per kg or \$0.0221 per kg net of catching.

11. The fixed differential promoted cooperation and drove efficiency through all sectors of the industry. It was transparent, fair, and predictable, as stakeholders understood that they needed to work within the parameters of the differential.
12. In 2015, the Chicken Farmers of Ontario (the “CFO”) disrupted price stability in British Columbia by implementing a new live pricing formula that included “efficiency adjustments”, which lowered the Ontario live price by taking into account expected production efficiencies and improvements in the costs of inputs for producers. The CFO took this action to address fundamental problems inherent in the previous Ontario live price methodology and to promote industry efficiency and competitiveness. Unfortunately, the changes to the Ontario live price formula and these efficiency adjustments were the root cause of most pricing issues across Canada.
13. In response to the new Ontario pricing model, and in order to provide maintain and increase returns to British Columbia growers, on May 29, 2017, the Chicken Board moved away from a fixed price differential to a more complicated model. Effective A-144, the British Columbia live price was based on:
 - Ontario Posted Price based on the historical weight category of 1.84 to 1.95 kg (as agreed by the PPAC on March 4, 2015)
 - Plus** 50% of the difference in feed costs per kilogram of live chicken between BC and Ontario (based on a 6 period rolling average)
 - Plus** 50% of the difference in chick costs per kilogram of live chicken between BC and Ontario (based on a 6 period rolling average)
 - Plus** 3.5 cents for catching costs. Changes to the cost of catching will be reflected in the pricing formula and must be submitted to the Board for approval prior to the beginning of a pricing period.
14. The rationale for the new model was to place less emphasis on the Ontario live price and to recognize the differences in feed and chick costs between British Columbia and Ontario. However, by introducing the factors of feed and chick into the live price, the Chicken Board provided new avenues for British Columbia industry stakeholders to offload costs on to processors.
15. On July 6, 2018, just 13 months later, the Chicken Board issued its “interim” formula, which increased the chick and feed differential from 50% to 75%. This change resulted in increased returns for British Columbia growers and an increased live price differential relative to Central Canada for British Columbia processors. This formula was to remain in place until the Chicken Board could establish a new long-term pricing structure.
16. Nearly two years later, this “interim” formula remains in place. The current formula builds on the same framework as the May 29, 2017 formula, but it has resulted in higher live price differentials

between British Columbia and Ontario than the previous formula and increased returns for British Columbia growers. The live price differential has been increasing in British Columbia to offset the efficiency adjustments in Ontario.¹ Said differently, British Columbia processors have been funding the Ontario efficiency adjustments for British Columbia growers.

17. Between periods A-129 and A-162, grower returns after feed and chick steadily increased.² Since period A-150, British Columbia growers have enjoyed similar returns after feed and chick when compared to Ontario growers. It has also been recognized that British Columbia growers have other farm operating cost advantages relative to Ontario growers. Despite this, growers continue to pressure processors to pay 100% of the feed and chick differential.

(2) Arbitrary components in the British Columbia live price formula

18. In the 2018 pricing appeal, the PPPABC pointed out a number of issues in the components of the live pricing formula.
19. The PPPABC demonstrated that using a six period rolling average to calculate the feed and chick differentials was causing wide fluctuations in the live price. In the Price Working Group (“PWG”), the BCCGA agreed. The Chicken Board followed the direction of the PWG and recently removed the six period rolling average from the live pricing formula.³ Despite this progress, there remain arbitrary components in the live pricing formula, primarily the feed and chick factor and the weight category. The feed and chick factor and comparator weight category are prone to manipulation and risk future pricing instability.
20. To this day, it is unclear why the Chicken Board chose to raise the feed and chick factor from 50% to 75% in the 2018 interim formula. Given the subjective nature of how the factor was implemented, and then changed, the PPPABC is concerned that pressure from growers or other stakeholders will lead to further unjustified increases at the processors’ expense. British Columbia growers have stated that they should receive 100% of the feed and chick differential. They will continue to push for further changes to the current formula, all of which will be at the expense of British Columbia processors.
21. In the 2018 appeal, the PPPABC provided data showing that the selection of the Ontario weight category of 2.45-2.65 kg for the pricing formula did not accurately reflect the production weight of chickens in British Columbia and therefore was not an appropriate weight category for comparison purposes. At the PWG, the PPPABC and BCCGA agreed that the weight category should be changed to 2.15-2.45 kg to accurately reflect British Columbia production and to provide a fair comparison versus Ontario. The Ontario live price for 2.45-2.65 kg weight category is \$0.02 per kg higher than the 2.15-2.45 kg weight category, and as a result inflates the live price in British Columbia. The PPPABC and BCCGA conducted additional work to amend the categories to provide fairness and transparency for both parties. Had the PWG continued, the

¹ Graph 1 – Revised live price differential between Ontario and British Columbia (periods A-129 to A-163).

² Graph 2 – Ontario and British Columbia grower returns (periods A-129 to A-163).

³ Chicken Board Pricing Order #154 (May 8, 2020).

PPPABC and BCCGA would have issued a joint recommendation to the Chicken Board on changing the weight category.

22. In the interim, beyond period A-163, there needs to be measures to prevent stakeholders from exploiting the weaknesses in the formula to improve the financial position of their respective sectors. However, the status quo is ultimately untenable for processors. It is the position of the PPPABC that there needs to be a long-term solution in the form of a fixed differential from the Ontario live price to provide stability to pricing.

B. Unilateral action by the Commission

(1) Exit from the linkage agreement

23. Since 1995, the returns received by hatching egg producers have been determined by a formula set through a linkage agreement. The March 14, 2016 Memorandum of Understanding between the Commission and Chicken Board provides the most recent linkage agreement (the “**MOU**”). The MOU included a requirement that neither party could withdraw from the MOU without the approval of the BCFIRB. The linkage agreement provided stability for the industry and prevented disputes over the chick price. Processors could then just focus on the live price of broiler chickens.
24. However, in breach of the MOU, the Commission announced its intention to withdraw from the linkage agreement and unilaterally changed factors within the linkage agreement. In a November 27, 2019 decision and Amending Order 26 dated November 28, 2019, the Commission imposed two changes:
- (a) the Commission removed the revenue streams for fowl⁴ and salvage eggs⁵ from the linkage agreement; and
 - (b) the Commission reduced the useful life of breeding hens from 58 weeks to 56 weeks in the linkage agreement.
- (the “**Linkage Amendments**”)
25. The Linkage Amendments increased hatching egg producer margins by increasing chick prices. In turn, this increased the price of live chicken paid by processors in British Columbia. The Commission made these changes due to broiler hatching egg producers believing that it was unfair that loyalty premium revenue was not included in the linkage agreement.

⁴ Fowl are spent broiler breeders no longer raised or used for the production of broiler hatching eggs. In British Columbia, the Commission regulates the price paid by processors to hatching egg producers for fowl. Processors then process and sell the fowl on the open market. Fowl is not supply managed.

⁵ Salvage eggs are eggs that are unfit for the hatchery. They include eggs that are underweight (below 52 grams) or have other issues such as double yolks and cracked shells. Salvage eggs are fit for human consumption but not hatchable. Hatching egg producers send salvage eggs to breakers for further processing, who pay hatching egg producers for these eggs.

26. In addition, the Commission is now advocating for a new cost of production formula, further complicating pricing discussions in British Columbia. This potentially puts processors in the position of negotiating multiple pricing formulas with multiple stakeholders. This is inefficient, and it will escalate live pricing in British Columbia.

(2) Instability from the Linkage Amendments

27. The first instability caused by the Linkage Amendments was the Commission's decision to remove the revenue streams that hatching egg producers receive from spent hens and salvage eggs from the linkage agreement. Beginning in period A-160, this increased the chick price by 1.01 cents per chick. This translates to 0.46 cents per kg of live chicken (based on a 2.2 kg live bird). Further, the removal of fowl revenue from the linkage agreement has opened up a new front of pricing disputes with respect to fowl pricing set by the Commission, which also affects the live price for mainstream broiler chickens.
28. Second, the Commission has adjusted the chick price based on changes in the useful life of a breeder flock. The useful life of a breeder flock moves up and down over time and does so in order to balance egg supply with quota allocations. The adjustment in A-160 was done in large part because the Commission overestimated industry growth at 106% of quota and placed too many breeders (despite the fact that hatcheries had requested a much lower level of placement). The result of reducing the useful life of breeding stock from 58 weeks to 56 weeks was an increase of 1.87 cents per chick, which equals 0.85 cents per kg of live chicken (based on a 2.2 kg live bird).
29. Combined, the Linkage Amendments resulted in an increase of 1.31 cents per kg for live chickens. If that is extended against the 2019 industry volume of 236,420,747 kgs of live birds, it represents an increased annualized cost to the industry of \$3,097,112. This cost is passed on 75% to the processors (\$2,322,834) and 25% to the growers (\$774,278). The Linkage Amendments are also leading to the return of increased chick price differentials between Ontario and British Columbia.⁶
30. Both the PPPABC and the BCCGA appealed the Linkage Amendments on the basis that the Commission made the Linkage Amendments without legal authority. Those appeals have been deferred pending the outcome of this supervisory review. As the PPPABC has noted before, the deferral decision has allowed the Commission to claim the benefits of the Linkage Amendments for three cycles now, without the Commission being held to account.
31. In years past, prior to the 2017 live pricing formula, the Linkage Amendments would have solely impacted hatching egg producers and growers. Now, the majority of changes to the linkage agreement flow through and impact processors, who were not a party to the dispute. This also means processors were paying loyalty premiums twice: first to broiler growers, and again through a higher live price as the Commission increased hatching egg producer margins to claim a portion of the premiums.

⁶ Graph 3 – Chick price differentials between Ontario and British Columbia (periods A-129 to A-163).

32. If the Commission believes it can unilaterally change the linkage agreement, the British Columbia chicken industry faces increased pricing instability. Two regulators now have the ability to alter the live pricing of chicken in British Columbia at the expense of processors. The Commission and Chicken Board have not demonstrated that they can effectively work together, let alone work with their downstream stakeholders who are paying for this dispute. The result is an increasingly unstable pricing environment without a coherent framework to move forward.

C. Margin issues for hatcheries

33. While the Commission has been aggressive in changing the linkage agreement to benefit hatching egg producers, it has not appropriately addressed the margin increase request from hatcheries. It has been over eight years since hatcheries last received an increase in margins, while they incur cost increases on an annual basis. The Commission has not implemented a systematic method to provide margin increases to hatcheries. Instead, for the past eight years, the Commission has allowed Ontario hatchery margin increases (in the Ontario live price) to flow through to hatching egg producers and broiler growers, but not to British Columbia hatcheries.⁷
34. More recently, the Commission offered an increased margin to the hatcheries, but their offer would result in costs being paid by downstream participants. The majority of the costs would flow to the processors through the live price formula. This would have forced British Columbia processors to pay for the Ontario hatchery margins twice: once by way of inclusion in the Ontario live price (the margin of which is shared by hatching egg producers and broiler growers), and second by way of an increased British Columbia live price due to an increased British Columbia chick price. As such, processors advised that they would not accept a hatchery increase if it meant even higher live prices.

D. Grower movement

35. In the June 9, 2010 supervisory decision on the Chicken Board's Pricing Related Recommendations (the "**2010 Supervisory Decision**"), the BCFIRB repealed assurance of supply. At the time, the PPPABC warned that an open sign-up system would result in growers leveraging this position to secure loyalty premiums. The BCFIRB panel in the 2010 Supervisory Decision believed that the risk of non-value premiums was "overstated".⁸
36. As predicted, soon after the 2010 Supervisory Decision, processors were forced to pay loyalty premiums to ensure a stable, predictable supply of chicken. Without the loyalty premiums, growers threatened to switch processors. It became a necessary cost of business for processors to pay loyalty premiums so that they could protect their ability to fulfill contracts on the open market with retailers and food service businesses.
37. Processors have recently stopped paying loyalty premiums. However, without assurance of supply, processors are vulnerable to significant grower movement, which could potentially force processors to pay loyalty premiums to fulfill customer contracts. This adds another layer to the

⁷ Graph 4 – Margins of British Columbia hatcheries versus Ontario hatcheries (periods A-129 to A-160), showing the margin gap between British Columbia hatcheries and Ontario hatcheries increasing over time.

⁸ 2010 Supervisory Decision at para. 58.

pricing instability caused indirectly by the current pricing formula. This would also result in uneven price increases for processors and uneven benefits for growers in British Columbia, and again hatching egg producers would seek a share of loyalty premiums.

II. Interim measures needed to create stability

(1) Rescind the Commission's unilateral changes

38. The BCFIRB should immediately rescind the Commission's unilateral changes to the linkage agreement in the Commission's November 27, 2019 decision and Amending Order 26 and prohibit the Commission from making further changes to the linkage agreement until the completion of the supervisory review.
39. The BCFIRB needs to return the economics of the British Columbia chicken industry to the state they were before the Commission's unilateral changes. The Commission's decision to exit the linkage agreement and pursue its own cost of production formula has further destabilized the industry. If each stakeholder – hatching egg producers, hatcheries, and broiler growers – develops and implements independent pricing schemes, it will put the competitiveness of the entire British Columbia industry at risk.
40. Without the intervention of the BCFIRB, the chicken industry risks further maneuvers by the Commission to interfere with the chick component of the live price. The current supervisory review will be more difficult if the Commission continues to make pricing a moving target.
41. The Linkage Amendments have created an additional \$3,097,112 in hatching egg industry margins, at a direct cost to other industry stakeholders. The live price differential between British Columbia and Ontario remains at historical highs, and with increased costs from COVID-19, processors cannot be forced to absorb the Commission's unilateral price increases.
42. The original premise of the Commission's decision to change the linkage agreement was that broiler growers were receiving premiums, while hatching egg producers were not. Premiums never provided an appropriate justification for the Commission to amend the linkage agreement, as premiums are unpredictable and not sustainable. The Commission knew of premiums when it entered into the MOU with the Chicken Board and agreed to the linkage agreement. Despite this, it acted without authority to change the linkage agreement for its own benefit and prejudice other industry stakeholders.
43. The PPPABC agrees with the BCCGA that the Linkage Amendments should be rescinded. The BCFIRB should not reward the Commission for its unilateral actions. By rescinding the Linkage Amendments, the BCFIRB would return the industry to the previous status quo during the supervisory review and provide a stable platform for long-term pricing negotiations.

(2) No further changes to the live pricing formula or inputs to the formula during the supervisory review

44. The PPPABC requests that the BCFIRB prevent any further changes to the factors in the live price formula until the supervisory review is resolved. This order should include a safety valve to

permit parties to apply to the BCFIRB for relief should there be extraordinary changes to market conditions. However, under no circumstances should this be construed as the PPPABC agreeing with the current pricing situation. The British Columbia chicken industry needs to work quickly to find a long-term pricing solution and locking down the price formula creates a motivation for the parties to act on this issue. The PPPABC's request is for the BCFIRB to facilitate stability in the industry and to prevent any further arbitrary changes to the formula. Processors cannot continue fighting multiple pricing battles with various stakeholders while they engage with the supervisory review and, more importantly, try to maintain their businesses during COVID-19.

(3) Fair distribution of Ontario live price changes

45. The BCFIRB should order that any changes in the Ontario live price formula resulting in increases and improvements British Columbia live price flow directly to British Columbia processors and hatcheries. The British Columbia processors have largely carried the financial burden of the efficiency adjustments as the Chicken Board has continued to increase the live price differential to offset these annual adjustments. For the past eight years, increases in Ontario hatchery margins have flowed to British Columbia hatching egg producers, rather than hatcheries.
46. The 75% feed and chick differential already over-compensates growers for the Ontario efficiency adjustments. Under the current British Columbia live pricing formula, if the efficiency adjustments are reduced, growers will receive a windfall, while British Columbia processors will continue to pay for efficiency adjustments. Instead, those adjustments should go directly to the processors and hatcheries. Absent a mechanism for fairly distributing future revisions to the Ontario live price, there will be further disputes and instability amongst stakeholders in the interim.

(4) Moratorium on grower movement

47. The BCFIRB needs to order a moratorium on grower movement pending the supervisory review. Without assurance of supply, growers will again threaten to move and demand loyalty premiums, which will destabilize the industry.
48. The dispute between hatching egg producers and growers about premiums adds another dimension to the issue. The Commission altered the linkage agreement to capture increases for hatching egg producers to capture the benefit of (former) loyalty premiums, which is a manipulation of the system. Should growers begin to move amongst processors, loyalty premiums may come back, which may lead to the Commission making additional countermoves to benefit hatching egg producers at the expense of other stakeholders.

49. To complement an interim prohibition on further changes to the linkage agreement, the BCFIRB should implement a moratorium on grower movement so that the industry can work through pricing issues from a stable foundation.

Yours truly,
Dentons Canada



Morgan L. Camley
Partner

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- cc. Robert Hrabinsky (counsel for the British Columbia Broiler Hatching Egg Commission)
cc. Claire Hunter, QC (counsel for the British Columbia Chicken Marketing Board)