



Appendix to June 26, 2020 Joint Submission
INTERIM PRICING AND LONG-TERM PRICING NEXT STEPS
SUBMISSION OF THE BC HATCHING EGG COMMISSION

New Approach to Pricing

Further to the joint approach to pricing by the Commission and the Chicken Board discussed in the joint submission, this is to confirm that the Commission continues, as per its June 8, 2020 letter: ...to work with its Alberta and Saskatchewan counterparts toward a common cost of production formula (COPF). A COPF that will match the processor and hatchery footprint across Western Canada while at the same time allowing for regional (provincial) variations like the egg COPF. The Alberta COPF framework, which includes consideration for Ontario, has been upheld on appeal in that province. All three provinces believe that a common COPF framework helps to balance the market power of processors and hatcheries. This initiative could also be a step toward a national COPF for hatching eggs. This remains a long-term objective of the Commission as outlined in its August 30, 2019 letter (attached) to Canadian Hatching Egg Producers. One which the Commission believes BC stakeholders should also take into consideration as part of a new approach to pricing and is another example of the in-depth examination required of BC pricing.

Status of the Linkage

The Commission's rationale for the removal of hatching egg revenue streams from the linkage was in accord with the sound marketing policy of the linkage, as noted in a December 18, 2019 letter to stakeholders:

It is the Commission's view that its November 27, 2019 correspondence to (BCFIRB), complete with a SAFETI analysis, fully explains the current situation with respect to the removal of revenue streams from the hatching egg COP. Neither the hatching egg nor chicken COP now include revenue streams that are not "costs".

It is also the Commission's view that the pricing adjustment after a reduction in the kill age was also in accord with the linkage, as again noted in the December 18, 2019 letter:

Kill age has been recorded as an input factor in the linkage calculation by Serecon since that time (Period A137). [May 15, 2016]

Subsequently, Bob Burden of Serecon, responsible for administering the linkage, confirmed that the kill age is a factor in linkage pricing. It should be noted that the inclusion of the kill age as an input factor in the linkage predates the current live price formula.

Revenue streams for growers, including premiums paid to them by processors, have never been a component in the linkage.



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The Commission has not had time to address the full extent of the processors' submissions on what they allege is the financial impact of recent Commission decisions on non-hatching egg sector stakeholders. As again the Commission is of the view that there is no evidence that pricing in the interim is unsustainable, a full examination should be part of the new approach to pricing process. However, the Commission is providing some analysis to illustrate that the financial considerations are not limited to the arguments put forward by the processors.

Premiums

1. The processors were quick to act arbitrarily in abandoning premiums, an estimated 3-cents/kg live weight pricing benefit to them. Using a single period (A-163) as an example, an allocation of 37,779,540 million kg live weight at 3 cents/kg equates to an approximate \$1.13 million in revenue loss to growers. The position of the Commission that premiums should be included in the linkage (dating back to 2013), has also been based on the premise that the posted live price plus the premiums was the actual price of chicken in BC. Now, the processors have not only abandoned premiums but are in effect asking BCFIRB to forestall at the expense of growers any regulatory or non-regulatory (grower movement) response to that change in chicken pricing for BC. The processors using 'assurance of supply' concerns as part of their argument about hatching egg revenue streams is contradictory as the Commission has retained assurance of supply for the processor-affiliated hatcheries through the Official Flock Plan.



Revenue Stream Issue - Fowl Price

2. The processors have also benefitted from the Commission instituting a 50-percent reduction in the spent fowl price from \$0.40/kg to \$0.20/kg live weight and directing a number of breeder flocks for rendering (the processing of which is compensated). This decrease in pricing has been responsive to processor concerns at a cost to hatching egg producers.

Spent fowl are a product regulated by the Commission and the fowl price has always been set independently by the Commission. Prior to COVID-19, the processors applied to the Commission requesting the fowl price be removed from the Consolidated Orders (presumably so the processors could set the price themselves). The Commission is awaiting the processors to supply more substantiation for the request. This drastic step would mean that this revenue stream would be subject to processor control, impacting directly on producer revenue and would reduce the benefit to growers if this revenue stream was still included in the hatching egg linkage cost of production (COP). While also losing the benefit if it were still in the linkage, processors would still have the advantage of a reduced or non-existent fowl price. The processors' opposition to the Commission's removal of this revenue stream and stating that the Commission is opening a "new front of pricing disputes" is contradicted by their own actions. Finally, it is also notable that the original increase to \$0.40/kg was in 2012 as part of an agreement to raise the hatchery margin. While the hatchery margin has not increased since then, neither has the fowl price and now the processors are arguing for a hatchery margin increase at the same time as requesting a fowl price decrease.

Hatchery Margin, Breeder Chick and Vaccine Pricing

3. Given the nature of the linkage, hatcheries are assessed as not being significantly affected by pricing during COVID-19. Both boards agree that the issue of the hatchery margin is outstanding and that the current linkage and live price formula present roadblocks. As per the Commission's June 8, 2020 letter, the hatchery margin must be addressed in conjunction with breeder chick and vaccine pricing, the latter two being significant revenue streams for the hatcheries. These must also be factored into any comparison of the hatchery margins in Ontario and BC as a straight comparison of the differential is misleading.

At the same time, breeder chick and vaccine costs are significant to both hatching egg producers and growers as these costs are calculated into the linkage and are reflected in the price paid by growers for saleable chicks. The boards have agreed that these three issues and the extensive background work that the Commission has already undertaken in consultation with the hatcheries should be factored into the new approach to pricing. Intended is a formula-based approach that could be similar in principle to the three-way COP arrangement in Ontario between hatching egg producers, hatcheries, and growers. This integrated approach to pricing – a new "linkage" based on the needs of the BC production sector – would address the processors' concerns about a multi-faceted approach to pricing with transparent and verifiable data. The only outstanding issue would be the appropriate live price at any given time.



Revenue Stream Issue - Kill Age

4. Even though the Commission reduced utilization to 100% of allocation for 2020, imports by hatcheries early in the year followed by the onset of COVID-19 have kept the kill age at 56 weeks. Consultation with the BC Egg Hatchery Association indicates that this will be the case for the foreseeable future. A further market recovery (the recent chicken allocation for Period A-165 is still two percent under base and an estimated four percent under what would have been the original, pre-COVID-19 allocation) could increase the kill age in time. So could a further reduction in imports by hatcheries. Although their recent cooperation and their obligations to their US suppliers are recognized, the amount of their imports to date in 2020 is still significantly higher than in the other western provinces in which the processors and their hatcheries operate. Year to date utilization of pro-rated TRQ to week ending May 23, 2020: BC – 107.9%, Alberta – 60.0%, Saskatchewan – 70.3% and Manitoba – 82.1%.

As the processors note in their submission, the kill age is a commonly used tool in the Canadian hatching egg industry to balance supply and demand. It is a matter of last resort as a lower kill age negatively impacts producer margins. Pricing in other jurisdictions based on hatching egg COPs is automatically adjusted accordingly, as provided for in the BC linkage. It is the Commission's view that here in BC the similar pricing change imply recognizes that a reduced kill age negatively impacts on the BC hatching egg linkage COP and equalizes the returns to producers and growers, as intended by the linkage. The kill age does not have a direct pricing impact on the hatcheries.

Similarly, if the kill age increases past 58 weeks (an efficiency goal of the Commission over time, originally starting in August 2020 before COVID-19), growers would also benefit from a shared increase in returns through the linkage. This would obviously not be the case if the position of the processors and growers is that hatching egg producers should have sole responsibility for increased or lowered production costs resulting from the kill age.

Although the BC kill age has historically been set at 58 weeks (and linkage pricing set accordingly), the actual direction of fowl for processing has operated within a two-week sleeve. For a variety of reasons, individual flocks could have been killed earlier or later than the projected 58 weeks. These operational, short-term differences do not result in changes to the official kill age used to calculate the linkage price. Production in 2019 was managed operationally until Period A-160 (commencing November 24, 2019), 46 weeks into the 58-week 2019 production year. The Commission determined then, after consultation with the hatcheries, that a "new normal" necessitated a reduction in the official kill age from 58 to 56 weeks. Domestic hatching egg production needed to be cut back for an extended period. This period was originally estimated by the Commission and the hatcheries as lasting until at least March 2020. COVID-19 has made that original estimate moot; with similar kill age and pricing adjustments also made in other provinces for the same reason. The Commission's analysis for regarding its 2018 utilization decision is outlined in detail in the attached May 29, 2020 report to stakeholders.

Revenue Stream Issue – Salvage Eggs

5. Due to COVID-19, the amount of salvage eggs that can be sent to the breaking market for processing (at a reduced price to producers) is restricted to historical levels by order of Egg Farmers of Canada. If that



historical revenue stream were again included in the linkage, it would result in a reduction to the standard figure of 0.175 of a cent in the linkage hatching egg calculation. This minimal benefit would be split between growers (25% and processors (75%) under the current live price formula and should be compared to the \$500,000 to date that hatching egg producers have paid in removing (dumping) hatching egg surplus to the chicken market and surplus to the historical average supplied to the breaking market. Finally, this current surplus in hatching eggs is increasingly from 2020 production at 100% utilization of allocation set long prior to COVID-19, not just the 106% utilization in 2019 that the processors note in their submission.

Revenue Streams – Consequences

6. It is the Commission's view that the actual impact on processors and growers from removing spent fowl and salvage egg revenue streams from the hatching egg linkage COP is less than argued. The recent negative impact on those revenue streams due to a reduction in fowl price, the rendering of flocks and the dumping of eggs is being borne by the hatching egg producers instead of being passed through the linkage. The Commission is seeking to have producers compensated for these losses through AgriRecovery. It might be important that the AgriRecovery application not be undermined by re-imposing a regulatory option, especially since the Commission has already stated in its May 22, 2020 letter to the BCCGA:

As noted in its decision of May 12, 2020, the Commission is not seeking to incorporate the current financial impact on hatching egg producers' revenue streams into the linkage COP.

Conclusion

As indicated in the submissions from the boards, an interim change to the current pricing *status quo* would require a full and in-depth examination of a multitude of factors. The impact of COVID-19 is also impacting on all stakeholders and the full, long-term impact of that crisis remains unknown. The Commission's position on pricing issues and the rationale for the decisions it has made to date have been transparent. In the interests of stability, and pending a new approach to pricing, the Commission intends remaining within the linkage and does not foresee at this time any changes to its linkage pricing pending the finalization of a new approach to pricing.