



Response to BCFIRB Questions Regarding: Regulation of Asian Hatching Egg Production

September 29, 2017

On August 25, 2017, the BC Farm Industry Review Board (BCFIRB) asked the BC Broiler Hatching Egg Commission certain questions regarding the regulation of Asian hatching egg production. The following represents the Commission's responses to those questions in addition to the information and analysis provided in its June 28, 2017 report to BCFIRB.

Question 1 – the Commission rationale for reconsidering its February 27, 2015 recommendation to increase regulation of Asian hatching egg production.

Historically, the February 27, 2015 recommendation conflicts with the Commission's position with respect to the appropriate regulation of this production. As evidenced by the history of this matter, industry stakeholders have also had shifting positions on this question, including by way of appeal of the February 2015 decision to establish a quota-based system.

The main focus of the appeal was the inherent limitations to production under a quota system. At the time, the Appellants argued that the imposition of a quota system would stifle the "diversity" that is so essential in that sector. Ultimately, BCFIRB agreed with the Appellants' position concerning the negative impact of a quota system on those who are not yet engaged in production, stating:

...the entry of Skye Hi and V3 into an unregulated (or not actively regulated) hatching egg industry in 2010. In the view of the panel, this is part of the industry's overall success story and is an indication of the growing strength of this small but important sector. It is not, as depicted by the Commission, Bradner and Coastline, a story of self-interest, market chaos and something to be condemned. (BCFIRB Decision, par. 116)

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The panel finds that regulating a return to fewer producers of Asian chicks than now exist is not consistent with sound marketing policy. In the current market, chicken growers have more choice of chick producers and there is increased opportunity for the development of variety within hatching egg breeds. We heard compelling arguments that diversity of producers in the Asian hatching egg sector provides for a more resilient marketplace, increased production efficiencies within the sector overall and protection in the event of outbreaks of disease or other disasters. In our view, the Commission's orders fail to give sufficient weight to the importance of diversity amongst producers in the further development of this sector. (BCFIRB Decision, par. 117)



Notwithstanding the foregoing, a key point here is that in its most recent review, the Commission – including “new” people and perspectives on the board – “wiped the slate clean, stepped back, took a fresh look by considering a range of options, consulted further with stakeholder about the industry.” The Commission outlined this clearly in its process documentation, including through developing and drafting a range of options for discussion with industry stakeholders. In accordance with the process direction of BCFIRB, the Commission tasked itself with thoroughly re-examining what was appropriate sound marketing policy with respect to the regulation of B.C. Asian hatching egg production in the context of the larger Asian breeder and chicken industry.

The February 2015 recommendation applied a traditional regulatory approach to Asian hatching egg production that was consistent with the overall regulation of the B.C. hatching egg industry. Intended objectives of increased regulation included providing stability and discipline to Asian hatching egg production, using a quota-based regime to ensure compliance with the requirements of Schedule 5 of the Commission’s General Orders (biosecurity, premises ID, etc.) and to resolve conflict. None of those objectives have been achieved to date. After re-engaging with all stakeholders, the Commission’s latest review identified serious concerns by other stakeholders about over-regulating this sector in light of current B.C., national (e.g., Ontario) and export opportunities and challenges facing the overall B.C. Asian chicken and hatching egg industry.

Other concerns included increasing the capitalization costs of the industry by issuing quota – benefitting and furthering the interests of those now in the industry (operating without quota) at the expense of future new entrants.

As noted in the Commission’s June 28, 2017 report, current (and likely future) participants in this sector are significantly integrated directly or in practice through established business relationships. The Commission heard evidence from hatching egg producers and Asian chicken processors that there may be more integration forthcoming. As well, market growth may be in the export of Asian chicken vs. significant growth in the domestic market. Whether a future standalone, new entrant producer-only participant – with or without quota – would be able to succeed in this industry structure and potential marketplace is an open question.

BCFIRB’s question with respect to pricing and production controls will be answered below but other developments such as the upcoming implementation of an administrative penalties system will enable the Commission to better address its concerns about Schedule 5 and related matters such as animal care. The intended use of quota issuance, suspension and retraction are no longer the only effective compliance measures for these important issues.

The Commission simply notes here that some Asian hatching egg producers remain non-compliant with Schedule 5 of its General Orders.



Question 2 – (a) rationale for not setting production controls at this time; (b) intention to issue “production” or “exemption” permits; and, (c) “capping” if production permits are issued.

With respect to (a), overall production levels for Asian chicken are set by the BC Chicken Marketing Board through that board's Specialty Markets Advisory Committee (SMAC). This is a true 'bottom up' approach in which market requirements are identified by the processors and approved by the SMAC. To date, that aggregate figure has always received the approval of Chicken Farmers of Canada (CFC). Once approved, that allocation is distributed as determined by the SMAC with the processors, specialty chicken growers and Asian breeder hatcheries concerned all signing and confirming production requirements on the Chicken Board's BC101 contract. Asian hatching egg producers – most of whom are “integrated” – therefore have a clear line of sight in determining the overall amount of production required and how that production is divided into the hatchery sector.

The Commission appreciates that production planning for hatching eggs is a longer-term exercise than for Asian chicken. However, the SMAC, Chicken Board and CFC do project annual production requirements from which Asian hatching egg production can be planned in much the same way as done by Canadian Hatching Egg Producers and the Commission for mainstream. This points to increased cooperation and information exchange and reporting between the Chicken Board, the Commission and hatcheries, which process the Commission is initiating as outlined in its June 28, 2017 report.

The Commission notes that the Asian hatching egg producers have themselves pointed out that strict production controls are standard in the mainstream hatching egg sector are not suitable for their production. This includes having no official flock schedule and establishing annual quota growth based on market share, with the latter led primarily by the processor and/or hatchery with which the producer is affiliated. This current system of processors dividing and procuring allocation, trickling this down through growers and hatcheries appears to be generally efficient and effective.

In terms of (b) and (c), the Commission intends to issue “exemption” vs. “production” permits. The Commission was prepared to look at “production permits” (and pricing) in its Option #2, however, consultation with stakeholders did not result in any uptake for that proposal which intent was to provide a level of stability and certainty. The Asian hatching egg producers seemingly because it did not offer “quota” and other stakeholders because increased regulation through capping and restricting production flexibility would adversely affect an evolving industry for the reasons outlined in our June 28, 2017 report. As noted above, production levels can already be effectively determined and managed through the Chicken Board's existing SMAC and BC101 processes.

It must be noted “exemption” as an alternative to the imposition of a quota system has been recognized by BCFIRB as a valid option as early as 2005, when it released its Specialty Review Report:



5.10. Exemptions

Exemptions provide a tool by which Boards may authorize individuals, or groups of individuals, to produce and/or market outside certain of the Boards' Orders. Exemption does not necessarily (or even usually) mean exemption from all regulation. Section 11 (1)(e) of the Act provides a Board with the power "to exempt from a determination or order a person or class of persons engaged in the production, packing, transporting, storing or marketing of a regulated product or a class, variety or grade of it." It is important that any exemptions provided be clear regarding which parts of the Orders are included in the exemption.

As the markets for supply managed products have evolved, average farm sizes have increased and the number of producers representing a significant majority of the production has decreased. Smaller production units can experience greater difficulty remaining viable as market pricing established by the Boards recognizes scale efficiencies through productivity variables in cost of production models. Smaller and mid-sized producers may exit the industry, generally by selling their quota to larger producers seeking to expand and having greater financial capacity by virtue of higher productivity and therefore higher margins under a fixed price scheme.

Many specialty producers are smaller producers serving local or regional markets, often by direct marketing efforts. For them, regulation – particularly regulation that is not calibrated to the realities of the class of production being regulated – can constrain their ability to produce and market their products. The administrative burden imposed by the regulation may tempt small producers to operate illegally outside the system or to simply quit. In the first case, illegal operation threatens the integrity of the regulated system while enforcement of the regulations can subject the Boards to unconstructive criticism. In the second case, withdrawing from operation may result in local direct market segments not being served, innovation being constrained and regional economic activity being curtailed. Sound marketing policy as articulated by FIRB and the Ministry is clear that markets must be served and innovation must be fostered.

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The Commission may wish to provide, if it has not already done so, a specific exemption for Asian specialty breeders. This exemption could take the form of an annually renewable license to produce Asian specialty breeders in any amount subject only to certain requirements such as humane production practices and marketing only for Asian specialty production.



Question 3 – rationale for not setting chick price at this time.

In its consultation phase the Commission identified two options (#1 and #2) in which it was prepared to consider COP pricing for B.C. Asian hatching egg producers. Pricing was supported by those producers but not by other stakeholders. The Commission also established that Ontario, B.C.'s potentially most significant competitor should it establish a federally-inspected specialty processing plant, does not provide a COP price for its Asian hatching eggs. Nor does the Commission think it likely that Alberta would be inclined to establish a COP price for Asian hatching eggs if such production should be (re-)established and maintained in that province.

A very compelling argument for the Commission is the existing "integrated" nature of the B.C. Asian hatching egg sector, most of it with direct relationships/affiliations with hatcheries; in some cases, also with processors. Presently, the Chicken Board has established COPs for pricing the two main types of Asian chicken (Taiwanese and Silkie). Chicken pricing is done every two periods and historically, the chick price charged by hatcheries is routinely incorporated into the COP for Asian chicken producers. Given the "integrated" nature of the Asian hatching egg sector, this in effect determines the hatching egg producer price. There was no evidence presented to the Commission that at this time there is any systemic pricing issue for the hatcheries or by extension "their" producers. Instead, significant pricing changes (upward) are generally accepted and absorbed into the chicken pricing COPs.

The Commission does not believe it a wise use of resources to expend mainstream producer monies to establish a COP pricing mechanism given the current industry structure. Even if you accept that there could be one or two standalone Asian hatching egg producers, how does the Commission establish a legitimate COP pricing system for such a small, diverse group of operations? A COP price could be an unnecessary and substantial financial burden to all producers, as well as becoming increasingly irrelevant if further integration (production/hatchery/processing) or consolidation occurs.

It appears to the Commission that the focus of pricing and market share competition is not between operations in their role as Asian hatching egg producers but rather between them (or their affiliates) as hatcheries. Even if the Commission were to also establish a chick price – again difficult to accomplish in the absence of a sound, transparent and fully compliant linkage between producer, hatchery and grower pricing – it should not be assumed that all competition between hatcheries in an evolving industry and market would cease. Nor should the potential ability of hatching egg producers in an integrated structure to access a hatchery margin be discounted if a pricing formula were to be considered in future.

The Chicken Board's overarching production planning and pricing processes do provide significant elements of the stable framework in which all industry stakeholders operate. Given that, the Commission remains of the view that setting a producer price and/or chick price – COP based or otherwise – is not required at this time. The Commission remains prepared to do either or both should future evidence indicate there are systemic or other reasons making it necessary to do so.



Question 4 – interface with the Chicken Board.

Some of the answers to this question were provided earlier in this submission.

The Commission and Chicken Board have met and had a very informed and positive discussion about the parameters and issues involved in regulating the B.C. Asian chicken and hatching egg sectors. Both boards agreed that the Chicken Board's COP pricing process for Asian chicken, SMAC and the BC101 contract fundamentally determine pricing and production for all the B.C. Asian chicken sector except for, potentially, any standalone Asian hatching egg producer. The SMAC "manages themselves." The Chicken Board also advised that it will not be accepting any new entrant specialty growers until after 2020, after its current transition period for organic growers to shift to mainstream or Asian chicken expires.

Neither board could see a substantive role for a separate Commission SMAC.

Given the current integration of the Asian hatching egg sector, neither board could see an immediate need for expansion of the BC101 form. As discussed above, production information routinely flows down to include Asian hatching egg hatcheries, which are signatories to production commitments in the BC101.

At the same time, both boards discussed how Asian hatching egg production and hatchery issues could be included in the Chicken Board's SMAC process; including in support of the longer-term production planning requirements for Asian hatching eggs. Adding a hatching egg representative to the SMAC (if not presently represented by an integrated hatching egg producer/hatchery/grower), or establishing an information exchange and reporting process were two of the options considered. It would be important for the Commission to be "in the loop" in some way to keep itself informed of sector issues as they continue to evolve. The boards will be further considering this matter at their respective upcoming board meetings.

On a larger note, the Commission and the Chicken Board used this interface discussion to recognize that as co-regulators of the B.C. chicken sector, it is incumbent on us to engage frequently and constructively on issues affecting that sector. This includes providing and receiving input about our respective strategic plans. The two boards are already planning to hold a joint strategy session to examine means and approaches through which the Commission and the Chicken Board can have a constructive, positive interface on an ongoing basis at upcoming board meetings.

Conclusion

In its latest review, the Commission "wiped the slate clean, stepped back, took a fresh look by considering a range of options, consulted further with stakeholders about the industry and used SAFETI to inform its recommendations." The Commission collectively and individually needed to conduct this examination due to the long and convoluted history of this issue, during which most Commission members and staff were not involved.

During this objective review, as evident by the options it was prepared to discuss, the Commission was open to a variety of solutions. Its June 28, 2017 recommendations represent its considered opinion as to what represents



sound marketing policy for the regulation of Asian hatching eggs at this present stage of the industry evolution. In making its recommendation, the Commission has met a key objective of the Specialty Review by accommodating specialty production; and doing so through regulation “calibrated to the realities of the class of production being regulated.”

The Commission will continue its efforts to inform itself of Asian hatching egg sector issues. Not only through its interface with the Chicken Board but through ongoing contact with and reporting from Asian hatching egg producers and hatcheries as well as continued supervision of Schedule 5 compliance. This will provide the information necessary for the Commission to monitor the sector – including for predatory practices – and enable it to reassess its position with respect to regulatory requirements if and as circumstances warrant.

In closing, the Commission stresses the need for some certainty to be applied to this issue. This would empower not only the Commission but stakeholders as well and enable the industry to move forward.

Yours truly,

A handwritten signature in black ink that reads "J. K. Collins".

Jim Collins, Chair
BC Broiler Hatching Egg Commission