Chicken Farmers of Canada
Les Producteurs de poulet du Canada

September 23, 2014

Ms. Nathalie Vanasse
Registrar
Farm Products Council of Canada
Central Experimental Farm
Building 59
960 Carling Ave.
Ottawa ON K1A 0C6

Re: Period A-127 Complaint – Chicken Farmers of Canada Reply to Compiled Summary of Evidence

Dear Ms. Vanasse:

CFC's reply to the FPCC Compiled Summary of Evidence respecting the Period A-127 complaint by CPEPC, FPPAC and RC will focus on the following subject areas:

- Process/timing issues.
- Main arguments by the complainants, notably arguments that:
  - The allocation for A-127 is too high and will cause future disruption to downstream stakeholders; and
  - The A-127 allocation, combined with tightness in chick availability, may lead to incorrect bird specifications and adverse competitive impacts on restaurants compared to retailers.
- Additional points raised by the complainants, notably that:
  - No processor requested an allocation in A-127 higher than base plus 3%;
  - Seasonality was not properly taken into account by CFC;
  - CFC's methodology for estimating domestic disappearance may not be accurate;
  - Chicken farmers with guaranteed margins ignore the advice and input of industry directors; and
  - CFC's governance should be changed to require a triple majority vote for quota allocations.

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To sum up, CFC's A-127 allocation decision is reasonable and should be approved by FPCC. CPEPC, FPPAC and RC have not substantiated their complaints with cogent evidence and arguments, and thus the complaints should be dismissed.

Process/Timing Issues

CFC agrees with the complainants that the timelines associated with chicken allocation complaints should in future be re-examined by FPCC. CFC's offers the following perspective and constructive suggestions on this issue:

- The timelines associated with chicken allocation complaints pose challenges to everyone concerned (including FPCC), taking into account the combination of the short chicken flock production life cycle and the need to allocate as close to the marketing period as possible.
- CFC supports an expedited procedure consistent with procedural fairness to deal with complaints respecting a specific chicken quota allocation.
- CFC also generally supports having a face-to-face process component with respect to complaints that are referred to a complaint panel. An appropriate face-to-face process allows FPCC members and staff to pose questions on matters that are of concern to them, and helps parties and interveners to properly address those concerns. A written process has disadvantages in this respect, and if done in multiple stages contributes to unnecessary delay.
- For reasons of procedural fairness and good governance, any meetings held by a complaint panel should be in presence of all the parties. Meeting in the presence of the parties can still allow for informality and for an expedited process.
- Council should be cautious about complaint information and arguments that were not before the decision-maker.

Reply to main arguments by CPEPC, FPPAC and RC

The claim by CPEPC, FPPAC and RC that the A-127 allocation is too high relies on conjecture, speculation and extraneous considerations rather than solid evidence. As addressed in more detail in CFC's presentation on September 3rd:

- There was ample evidence before the CFC Board when Period A-127 was set supporting the opportunity for responsible, balanced growth to satisfy increased market demand.
- The complainants cite market conditions in previous periods without addressing fundamental differences relative to the market conditions when Period A-127 was set, notably, in relation to such market indicators as:
  - wholesale prices,
  - storage stocks,

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  - processor margins, and
  - the competitive position of chicken relative to other meats.
- Likewise, the concerns expressed about potential weakness in the market are contradicted by the bullish statements by CPEPC and FPPAC in the process leading to the setting of A-127. These statements cannot be reconciled with the claim that the A-127 allocation will cause disruption in the marketplace.
- Supply management is about taking advantage of growth opportunities when the right conditions exist. Supply management is not about curtailing production to enhance the margins of industry stakeholders.
- It must be kept in mind that, although A-127 was set 4.25 percent above base:
  - Period A-127 will still be the lowest production period of the year as a result of the base adjustments reflecting seasonality to establish a bell curve;
  - Period A-127 will only be 2.8% percent higher when compared to the equivalent period of the previous year;
  - At the urging of downstream stakeholders, chicken production was curtailed earlier in the year (notably, A-123, A-124 and A-125), and thus A-127 largely involved making up for this shortfall in response to extremely positive market indicators. This is not evidence of a "boom and bust cycle". The reality is that downstream stakeholders were unduly pessimistic earlier in the year, and Directors made appropriate, responsible evidence-based upward adjustments for A-127.

To further elaborate on the last point, it is useful to consider the conservative allocations set, at the urging of downstream stakeholders in A-123, A-124 and A-125.

<u>A-123 (March 23, 2014 - May 17, 2014)</u>

- initial requests from the provinces: 2.7% above base (provinces ranging from 2% to 3.1% above base;
- CPEPC requested 0% above base;
- FPPAC requested 1.5% above base;
- RC requested 1.2% above base;
- Domestic allocation was set at 1.5% over base;
- CPEPC, FPPAC and RC Directors voted in favour.

<u>A-124 (May 18, 2014 - July 12, 2014)</u>

- initial requests from the provinces: 1.8% above base (provinces ranging from 1% to 2.5% above base;
- CPEPC request was split between 2% below base and 0% above base;

- FPPAC requested 0.25% above base;
- RC requested 0% above base;
- Domestic allocation was set at 0% above base;
- CPEPC, FPPAC and RC Directors voted in favour.

A-125 (July 13, 2014 - September 6, 2014)

- initial requests from the provinces: 2.3% above base (provinces ranging from 2% to 3% above base;
- CPEPC requested 0.5% below base;
- FPPAC requested 0.5% below base;
- RC requested 1.6% below base;
- Domestic allocation was set at 1% over base;
- CPEPC, FPPAC and RC Directors voted against.

To respond to another issue, it is speculative for RC to claim that chick supply issues will lead to out-of-spec chicken production. It should be added that chicken production specifications are addressed by individual processors working with individual chicken producers in light of customer demands, and are not controlled by CFC.

RC also expresses concern about facing competition from retailers as a consequence of how restaurant pricing formulas work. However, CFC's mandate in chicken allocations is to meet market needs. It would be quite improper for CFC to adjust allocations with the goal of reducing competition between restaurants and retailers.

Reply to new positions advanced by CPEPC, FPPAC and RC

The FPCC Compiled Summary of Evidence indicates that CPEPC, FPPAC and RC made a number of additional points during and after the September 3rd meeting that were not raised in their initial complaints, and that CFC did not previously have an opportunity to respond to.

These additional points should be approached by Council with great caution, since they were also not addressed in the consideration by CFC Directors of the A-127 allocation.

One such point, advanced by CPEPC, is that no processor submitted a requirement higher than base plus 3%. This statement must be viewed with caution in light of the submissions by Manitoba Chicken Producers in response to the complaint, and the gaps in information about what individual processors were recommending in terms of market requirements. Furthermore, the allocation number CPEPC put forward was 1.75% above base, not 3%. To put the CPEPC recommendation into perspective, 1.75% above base would translate into an increase of only 0.3% compared to the equivalent period in the previous year.

The complainants also suggest that seasonality was not considered in the setting of the A-127 allocation. This is simply incorrect. It is well known that demand for chicken varies throughout the year, typically experiencing a reduction at certain times of the year such as December. Seasonality is factored into setting the base numbers and is something CFC Directors are quite familiar with. It is in light of seasonality adjustments that A-127 will be the lowest production period in the year despite being set at 4.25% above base.

The complainants call into question the sources of data used by CFC to calculate domestic disappearance and put forward alternative figures (never seen by CFC before) to estimate domestic disappearance. These new points are highly problematic.

For one thing, the methodology used by CFC to calculate domestic disappearance has been used and generally accepted at CFC board meetings, and in the industry generally, for many years. The data used to calculate domestic disappearance is publicly available through AAFC (storage stocks, imports and exports) and CFC (production). As is the case with most data, the numbers are not perfect, but they are recognized as the best available means of tracking overall domestic disappearance.

Also, strength in domestic disappearance numbers corresponds with strength in other market indicators, reinforcing the overall view of CFC Directors that a meaningful growth in allocation is appropriate in A-127.

Furthermore, it would be a dangerous precedent to allow the complainants to replace the long-established methodology for domestic disappearance with a new and untested methodology that has not been considered or even discussed by CFC Directors. The complainants are free to suggest changes to how domestic disappearance is calculated, but they should raise their concerns with CFC Directors first, rather than after the fact following a complaint to FPCC.

Finally, it would appear that the complainants have made arbitrary adjustments to domestic disappearance calculations to make up for data source time lags in the established domestic disappearance methodology. These proposed adjustments would need to be carefully analyzed to make sure that they do not fundamentally distort a well-established and useful, albeit imperfect, market indicator.

Next, the complainants claim that: “Farmers, who have a guaranteed margin, ignore the input of all Directors and organizations”.

For several reasons, there is no substance to this claim:

- For one thing, in the quota allocation process downstream stakeholders are the first to provide their market requirements. These proposals are shared with provincial boards prior to the boards providing their own market requirements to CFC. In other words, consideration of input from downstream stakeholders is built into the front end of the process. Downstream stakeholder input is in turn frequently referred to in quota allocation proposals to CFC by provincial boards.
- In addition, the bottom up process is designed to encourage processors to collaborate with provincial boards in their province in assessing market requirements. In recent years, however, processors in certain provinces have declined to pursue this opportunity, a factor that weakens the claim about stakeholder input being disregarded.
- Downstream stakeholders also have input when the allocation is set. They have seats at the CFC Directors' table and their voice is heard. As A-127 illustrates, downstream stakeholder input frequently results in adjustments to the overall allocation. In A-127, the growth in allocation came in at an overall number of 4.25% above base that was considerably lower than the 5% increase sought by a number of provinces. The same pattern can be seen in other periods, as the earlier snapshot respecting A-123 to A-125 shows. In other words, CFC Directors listen to input from various sources in the effort to arrive at a balanced and considered allocation decision.
- The reference to farmers having a guaranteed margin is off the mark. CFC does not have any authority in respect of the price of live chicken or the margins producers receive. These are provincial matters. It is also ironic for downstream stakeholders to be criticizing how live chicken is priced, given their role in the shaping of existing provincial live chicken pricing mechanisms.

Equally without merit is the complainants' post-complaint request "that the CFC's governance be amended to require a triple majority for setting quota allocations".

First, this requested relief is improper since it goes well beyond the scope of the initial complaints. As a consequence, only CFC and the active interveners have notice of this attempted shift in focus of the appeal. FPCC's focus should be on whether the complainants have demonstrated that the A-127 allocation is unreasonable, not on extraneous post-complaint remarks.

Second, to alter voting requirements for quota allocations would require amendments to the Operating Agreement that forms part of the Federal-Provincial Agreement for Chicken. Amendments to the Operating Agreement require unanimous agreement of provincial supervisory boards and provincial commodity boards. In other words, this is a signatory issue.

Third, even if it was properly before FPCC, the request for a downstream stakeholder veto could not be considered without addressing the systemic attempts by downstream stakeholders to curtail chicken industry growth to enhance their margins or limit competition between industry sectors.

CFC appreciates this opportunity to provide reply submission to FPCC. We do not anticipate the need to provide any input in respect of the final reply by the complainants, provided no new issues or evidence are raised that we could not have anticipated.

Yours truly,

Mike Dungate
Executive Director

c.c. Robin Horel, President and CEO, CPEPC
Robert DeValk, General Manager, FPPAC
Rick Hall, Federal Policy Director, Restaurants Canada