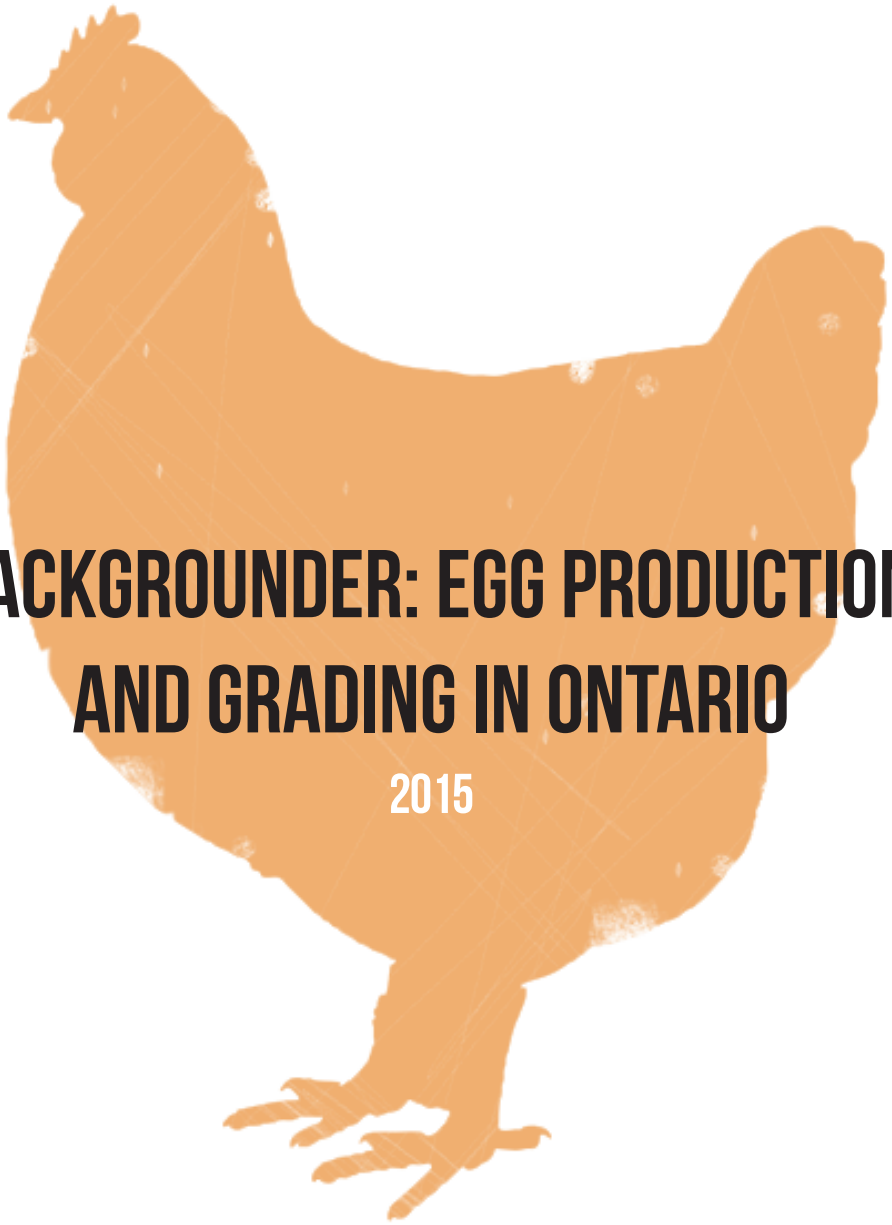

BACKGROUNDER: EGG PRODUCTION AND GRADING IN ONTARIO

2015

Farms at WORK

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1. **Introduction**

Farms at Work (FAW) is committed to keeping farmland healthy and active in east central Ontario. As such, FAW seeks to support the existing farming community and attract new farmers to the region by creating economic opportunities for farmers and developing infrastructure for food and farming enterprises.

The purpose of this report is to provide background information to support building capacity for local food production and distribution, thereby increasing the accessibility of local foods – specifically eggs. This is in response to recent interest in the feasibility of small-scale egg grading stations that would make it easier for small flock producers to access egg grading facilities, allowing them to sell at locations beyond the farm gate. It brings together background information about the egg production industry, supply management and the flow of production, egg grading regulations, and the implications for farmers and eaters.

2. **Background & Context**

2.1 **Egg Industry Organization: Supply Management**

Along with other agricultural commodities, the egg industry in Canada operates under a national supply management system. Supply management of eggs was introduced in 1972 in order to provide fair returns to producers and reasonably priced supply to consumers (OMAFRA, 2014). The system functions by matching the total supply (domestic and imported) of a product in Canada with the total demand, and dividing up the rights of production (referred to as quota) between producers (Agriculture and Agri-Food Canada, 1999). The Egg Farmers of Canada (EFC) (previously the Canadian Egg Marketing Agency) administers the national system for eggs by determining the annual domestic egg supply and dividing it among the provinces. It employs disciplines to prevent producers from producing in excess of their quotas, and tariff rate quotas to control imports by applying high tariffs above specific levels (OMAFRA, 2014).

Each commodity under supply management has a provincial board responsible for regulating the production and marketing of the commodity. In Ontario, Egg Farmers of Ontario (EFO) allocates Ontario's share of the domestic egg supply to producers, and sets the prices paid by graders to producers for certain grades and sizes of eggs (OMAFRA, 2014 & Farm Credit Canada, 2012). Retailers then buy eggs from graders at a price negotiated between the two parties. Whole eggs produced in excess of the table market are re-purchased by the EFO or EFC at a price that is derived based on cost of production, and then sold at a subsidized rate to processors (OMAFRA, 2014).

The EFO is responsible to the Ontario Farm Products Marketing Commission, a branch of the government that is intended to ensure that commodity boards such as the EFO are responding fairly to the broad demand in the marketplace. .. The Commission administers the legislation and regulations under the Farm Products Marketing Act (FPMA). The Commission is comprised of private citizens appointed by the Lieutenant Governor in Council (currently a chair and six members). The Commission is in turn

accountable to the Minister of Agriculture, who is accountable to the Cabinet and Legislature (OMAFRA, 2015).

2.2 **National & Provincial Context: Numbers and Trends**

Canada's egg industry has experienced slow but steady growth since the early 2000s. From 2000 to 2010, the industry expanded approximately 1.5% each year. In 2013, Canada was home to 1,021 egg farmers that produced approximately 585 million dozen eggs (Egg Farmers of Canada, 2013). Retail egg sales are also in a trend of growth: 2013 was the 7th straight year of increase in retail sale of eggs (The Poultry Site, 2013). Similar to other farm commodities, there is a general trend of consolidation in Canadian egg operations; the number of egg farms is declining as production facilities increase in size. One of the consequences of farm consolidation is that the level of investment in the business has made it more difficult for farmers to pass their operations on to the next generation or sell their operation to a new entrant to the business.

Egg production levels vary across the country, with the majority of eggs being produced in the central region of Canada (e.g. Ontario was allocated almost 37% of the total federal quota in 2014). There are 325 quota-holding egg farmers in Ontario, of which the average egg farmer owns 23,581 laying hens (Egg Farmers of Ontario, 2013). Non-quota holding egg farmers, while there are many, make up a small proportion of the total egg production.

2.3 **Industry Structure: Egg Production in Canada**

This report focuses mainly on egg production and grading, but several other sectors exist in the Canadian egg industry. For example, some operations specialize in breeding, hatching, or producing pullets, and there are special plants for "breaking" eggs (processing) and further processing. While many farms/farmers focus on one sector of the industry, larger corporations sometimes vertically integrate more than one sector into their business model. For example, Burnbrae Farms operates egg production, grading and further processing facilities in Ontario (Burnbrae Farms, 2015).

Egg Grading

The egg grading system is standardized across Canada and regulated by Agriculture and Agri-Food Canada to meet food safety requirements. Egg Regulations, under the Canada Agriculture Products Act, dictate the laws around egg grading, packing, marking and inspection of eggs and international and interprovincial trade in eggs. Under the regulations, any egg that is sold from a location other than the farm gate must be graded in a federally registered egg grading station that is inspected by the Canadian Food Inspection Agency (CFIA). This has many implications, one of which is that it restricts the market outlets available for farmers who do not have access to a grading station. In 2013, there were 203 federally registered egg-grading stations in Canada (Agriculture and Agri-Food Canada, 2013). The process itself includes receiving, washing, candling, weighing, packing and storing eggs. Eggs are graded according to interior quality, weight, cleanliness and shell construction and receive the following grades (Farm Credit Canada, 2012):

Grade A: sold at retail markets for household use
Grade B: used for commercial breaking or further processing
Grade C: sold to commercial processors for further processing

Canada A eggs (consumer grade) must be clean, and free of leaks, cracks or other defects. These eggs are further sorted by weight into the size categories of Jumbo, Extra Large, Large, Medium, Small and Peewee (Agriculture and Agri-Food Canada, 2013).

After the egg grading process, table eggs are sold to a retailer at a price negotiated between the two parties (graders and retailers). Sometimes the egg farmer is also the retailer, and the eggs are sold from the farmer, to the grader, and back again. However, in most cases, large grading stations do not offer custom egg grading, because the scale of their operations makes it difficult (and inefficient) to track eggs from different farms. One consequence of this reality is that the farmer does not necessarily receive back the same eggs that they produced (EFO, 2015). This model is problematic for small farmers who produce for a niche market (e.g. free range, organic) and rely on consumers paying a premium to support their farming business model..

Egg Processing

According to the EFO, at any given time in the market, approximately 75% of graded shell eggs are sold as table eggs (e.g. whole eggs at grocery stores), while 25% are sold as breaker eggs (for further processing or industry eggs) (Egg Farmers of Ontario, 2015). This does not mean that 25% of graded eggs have broken shells when they are graded – rather, that 25% of all eggs suitable for human consumption are intentionally "broken" in processing plants, where eggs are processed into liquid, frozen or other processed egg products for sale to restaurants, hotels, institutions and further processors, or exported. Interestingly, processed eggs make up nearly the entirety of Canada's egg exports, the majority of which are sold to the United States, Germany and Russia (Farm Credit Canada, 2012). There are significantly fewer egg processing facilities in Canada than there are grading stations; in 2013, there were 15 federally registered processing plants and 203 grading stations (Agriculture and Agri-Food Canada, 2013). "Broken" eggs that go for further processing are used in value-added goods and may include products such as baked goods, pasta, mayonnaise and frozen meals. Eggs may also be used to make shampoo, pet foods and adhesives, or have certain proteins extracted for use in pharmaceuticals (Farm Credit Canada, 2012).

Levy System for Graded Eggs

Another important piece of the egg puzzle is the role of the Egg Farmers of Ontario (EFO) and the levy system for graded eggs. For every egg that is graded and sold in Ontario, a levy fee is paid to the EFO (the provincial egg board). In the last 5 years, the levy has ranged between 25.5 and 39.25 cents per dozen, and is currently (2015) at 31.25 cents (Egg Farmers of Ontario, 2015). The majority of levy fees collected are used to support a surplus removal program; shell eggs produced in excess of table needs are sold into the processing market stream at volatile world prices. In other words, the levy subsidizes breaker eggs, which are sold for a minimum price that is much less than table eggs (e.g. in 2014, breaker eggs were sold to processors at 69-95 cents per dozen, depending on their size) (Egg Farmers of Ontario, 2015).

"Grandfathered-In": What are the exceptions?

Exceptions can be found to nearly every "rule" in the egg industry. Small farmers who were grandfathered into the system in the 1980's and grade **only their own eggs** are exempt from paying levy fees and from following all of the current egg grading regulations. However, if they decide to custom grade eggs from other farmers, they lose their exemption and must pay levy fees on all of the eggs that are graded at their station (theirs and others).

This is relevant to custom egg grading options in east central Ontario because many of the federally registered egg grading stations that exist on small farms have been in operation for many decades (before grading regulations and the egg boards existed) and as such, are exempt from paying levy fees. When asked in the course of this research if they are interested in offering custom grading, they have indicated that they are not, as it would have negative impacts on their current business. For example, one of the farmer/graders in central Ontario raises a small flock as a part of a diversified operation. The operation was grandfathered into the levy system, and therefore they do not pay levy fees even though they grade their own eggs and take them to two markets. The profit margin on their eggs is 50 cents a dozen. If they offered custom grading, they would lose their exemption and the margin would shrink to ~18 cents a dozen. This exemption provides grandfathered operations with a significant business advantage, and makes it unlikely that they will take in eggs for custom grading.

2.4 **Small Egg Producers and the Quota System**

In the egg industry, supply management stabilizes prices for producers and consumers, and stabilizes supply for processors (Farm Credit Canada, 2012). However, while there are tangible benefits of supply management for farmers who own quota, the system creates significant barriers for both new and small egg farmers. As a *new* Ontario egg farmer, a producer has two options:

a) buy into the quota system (purchasing quota from another farmer) or

b) keep a small flock of a maximum of 99 birds

The EFO New Entrant Program has, since 2011, developed a 'New Entrant Quota Loan Pool' through which new quota farmers may be loaned extra quota space for the first 20 years of operation, 'repaid' by 10% of the loan quota volume per year. (see EFO's New Entrant Application 2011).

The economics of these options are problematic; buying into the quota system requires a very significant financial investment, while the small flocks allowed under exemptions are often too small to provide a reasonable return for effort.. The lack of a medium-scale option significantly limits the choices that egg producers have for their operations.

The Cost of Quota

In 2012, the cost of one "laying slot" of quota was $375 (Food Security Research Network, 2012). The economics of the egg production business are such that individual Ontario egg farmers own an average of more than 23,000 hens. In other words, the economics of the system encourages large-scale laying operations and heavy investment.

The quota-holders that were spoken to for this project were hesitant to speak openly about their operations. One central Ontario farmer of 30,000 hens is cynical because people call their family farm a factory farm. In reality, they say, they have no choice, because it is impossible to make money at any other scale. Egg farmers (especially those who have produced eggs for generations) are bound by the economic realities of the system in which they work.

Small Flock Exemptions & Grandfather Flock Policies

As an egg producer in Canada, the only alternative to buying quota is to raise a small flock that is exempt from the supply management system. In Ontario, small flock egg producers fall into one of two categories: they can raise up to 99 hens under a Small Flock Exemption, or up to 499 hens under the Grandfather Flock Policy. The small flock exemption is an option for any farmer, while to qualify for a grandfather flock exemption, a farmer must meet the following criteria (EFO, 2014):

> *A producer who can establish to the satisfaction of the local Board that the producer was in possession of 500 fowl or less on or before the 5th day of July, 1983 and who has since then been in continuous possession of fowl for bona fide commercial purposes as determined by the local Board on said premises, the beneficial ownership of which has not changed, and on which premises no other fowl are possessed, may apply to the local Board for an exemption from the quota requirements.*

Grandfather flocks are non-transferable (cannot be sold). However, intergenerational transfers are permitted; the flock may be passed on within the same family, on the same property (Egg Farmers of Ontario, 2015).

Impact of Small Flock Production

As previously mentioned, there are many more small flocks in Canada than quota-holding producers. In Ontario, there are about 1500 small flock exemption egg farmers compared to 325 quota holders. However, their production levels are so much lower than quota producers that they produce only 4% of the eggs in the province (see table below):

Market Share of Quota-Holding and Small Flock Producers in Ontario

	# of Producers	# of Hens per Farm	% of Egg Production
Quota-Holders	325	23,581	96%
Small Flock Exemption	~1000	1-99	4%
Grandfather Flocks	~500	1-499	

(Egg Farmers of Canada, 2013 & Egg Farmers of Ontario, 2015)

Market Outlets: Where are eggs sold?

Most of the eggs produced for the quota system are sold to egg grading stations at minimum standard rates set by the commodity production system. These prices are generally not high enough for small farmers to make a profit. For this reason, most farmers with a small flock exemption or grandfathered flock exemption sell their eggs from their farm property, where they can avoid the added cost of egg grading. They often

tap into a local specialty niche market (e.g. free-range, certified organic, heritage breeds). However, some small farmers also have their own on-farm grading station and can legally sell their eggs at farmers' markets.