IN THE MATTER OF AN ARBITRATION

BETWEEN:

HARTUNG BROTHERS INC.

Applicant

- and -

ONTARIO PROCESSING VEGETABLE GROWERS

Respondent

Appearances:

For the Applicant:

Dan Hartung
Dan Layton
Kevin Talbot

For the Respondent:

Al Krueger
John Lugtigheid
John Mumford
Francis Dobbelaar
Frank Schonberger

DECISION AND REASONS

The Arbitration

1. I was appointed sole arbitrator in this matter by the Farm Products Marketing Commission pursuant to section 21 of the Regulations to the Farm Products Marketing Act to arbitrate the price of Hand Harvest and Machine Harvest cucumbers in Ontario for 2015.

2. The arbitration was held in London, Ontario on January 15, 2015 and I rendered an Award on January 20, 2015 selecting the final offers of the Respondent Ontario Processing Vegetable Growers for Hand Harvest and Machine Harvest.

Positions of the Parties

3. **The Appellant (HBI) submits that:**

Hand Harvest

a) The HBI offer is an increase of 8.5% and (i) covers all increases in crop input costs including those related to changes in the exchange rate and (ii) provides the growers with a margin enhancement of 4% to increase the growers profitability.

b) HBI has made substantial capital investments for benefit of the growers by expanding capacity to market one of the most profitable crops

Crop Input Cost

c) Since 2010, HBI has managed daily crop flow by establishing the maximum number of acres for a grower to plant and by providing for and enforcing split planting. These measures will improve crop yield for the growers and increase yields by 1.85%. An increase in yields will decrease growers expenses by decreasing the acreage to be planted. The crop input analysis indicates an increase in yields of $0.36 bu.

d) The objective of measuring daily crop flow is to have fewer crops in the field to improve the growers economics. Yield assumptions have increased from .540 bu / acre to .550.

e) The HBI offer is based on a cost model the parties adopted to measure the year-to-year difference of changes in input costs.

f) Input cost increases in the offer are $.363%, which offset input increases.

Grower Margin Enhancement

g) The HBI offer provides for a 4% increase in grower profit margin to recognize Ontario's competitiveness and changes in the exchange rate.

h) The crop input cost adjustment and grower margin enhancement result in a final offer of $0.716 for Hand Harvest, which is consistent with how settlements were made in past years.

i) The growers have no currency risk as their purchases and sales are in Canadian dollars.

Machine Harvest

j) HBI makes submissions similar to its Hand Harvest submissions in support of its offer on Machine Harvest relating to cost input increases and grower margin enhancement. The increase is 8.2%.

k) The total input costs increase is $0.202 per bu.

l) Yield assumptions have increased by 6.25% from 320 bu/acre to 340 bu/acre and as in the case with Hand Harvest, this increase will reduce the growers expenses by requiring less planted acreage.

Conclusions

m) The growers offer on an adjustment in the 2015 price based on exchange rate changes from 2014 in excess of the affect on input costs " makes no economic sense "

n) The HBI offer keeps the growers whole on a costs basis with inputs "trued up" including currency exchange rates.

o) The offer allows HBI to meet the needs of its processing customers for competitive pricing.

4. The Respondent (growers) submit that:

Hand Harvest

a) The prices should increase by 13.5 % based on two components; (i) the Cost of Production (COP) used by the parties to measure the effect of changes in the growers cost of producing cucumbers from year to year and (ii) an agreement reached during negotiations in 2014 as to how currency changes would be accounted for in the future.

b) HBI buys cucumbers in Ontario and the US and sells to processors " almost entirely in the United States "

c) Ontario is the dominant supplier of Hand Harvest cucumbers due to several factors including a reliable labour source.

d) The parties have had annual price discussions for the last 7 years focused on COP increases and currency changes in Canadian and US dollars.

Cost of Production

e) COP shows year to year changes in the major grower crop input costs. The largest part of the increase is increased labour costs, due to the increase in the Ontario minimum wage introduced in Ontario shortly after the 2014 agreement was reached.

f) HBI offered to increase prices to offset the increase in production costs to an extent that would cover approximately one third of the increase due to the minimum wage increase. The offer was on the condition that when the parties compared year-to-year labour costs, both 2014 and 2015 would show a minimum wage of $11 so that for 2015 pricing, there would be no change in labour costs reflected in the COP. Growers honoured the 2014 agreement and absorbed the increase in labour costs with the expectation that it would be covered in the 2015 agreement.

g) Input costs in the COP are based on HBI's information as the components are supplied by HBI under contract which requires the growers to buy from HBI. An example is seed costs. HBI purchases seed from US suppliers in U.S. currency. In past negotiations, to convert from US currency to Canadian currency which is used to sell to Canadian growers, the parties have used the October/November average exchange rate from the most recent year.

h) The HBI offer discounts cost increases and currency changes which have been influential factors in past negotiations and the offer expects growers to "true up" only when it favours HBI

Currency

i) A currency "true up" arose in 2011 when the Canadian dollar rose significantly compared to the US dollar and HBI requested a price reduction to recognize its significant US customer base. This resulted in a 11.8 % decrease in price notwithstanding a 1.7% increase in grower costs.

j) In 2014, growers agreed to a price reduction in consideration of an agreement that they would true up currency annually based on the October/November average using the prior years October/November average as a base. The parties used this calculation in prior years.

k) The increased purchasing power of the US dollar against the Canadian dollar means the increase in costs is effectively 5.1% of the grower offer.

Machine Harvest

l) The increase is 8.8% using a calculation of COP similar to Hand Harvest with land costs being more significant than Hand Harvest because of the changes in land costs.

m) The increase in COP is due to two main factors, first, the increase in seed costs sold by HBI to the growers pursuant to contracts required by HBI; seed is purchased by HBI in the US, adjusted for currency using the October /November average exchange rate and then sold to the growers in Canadian dollars. The cost increase in seed costs adds $32.50 per acre to the growers costs. The second factor in the COP increase was the cost increase in harvest costs, which are paid by the growers to HBI. HBI requested an increase in harvest costs and an increase from $285/ to $370 per acre was settled.

n) Most of the cost increases in Machine Harvest were pass through costs to HBI.

Conclusions

o) The growers offer is logical and consistent with historical pricing practices which are discounted in the HBI offer with respect to COP and currency.

p) Fundamental principles of fairness dictate that factors influencing prices in the past should continue now.

Decision and Reasons

5. As stated in my Award dated January 20, 2015, after careful consideration of the written submissions of the parties and the oral hearing at the arbitration, I selected the final offers of the Respondent, Ontario Processing Vegetable Growers for Hand Harvest and Machine Harvest cucumbers for 2015.

6. In making my Decision, I accept the submissions of the growers including:

   a) the offer is consistent with the principles on COP and currency exchange on which previous agreements have been based;

   b) the HBI offer introduced new concepts to the cost of production calculation such as crop flow analysis and growth margin enhancement which had not been used in previous negotiations;

   c) it is not conclusively established that grower yields are increasing with the resulting decrease in grower costs;

   d) the increases in input costs are primarily flow through costs in that they are sourced through HBI and passed on to the growers;

   e) in 2014 the growers agreed to absorb the labour cost increase in the expectation the currency exchange would be reflected in the 2015 agreement based on understandings over the last 7 years on dealing with currency exchange. The growers offer is based on this understanding.

   f) for these reasons, I select the final offers of the growers for Hand Harvest and Machine Harvest as being fair and reasonable to the parties in the circumstances.

"Peter G. Cathcart"
Peter G. Cathcart, Q.C.
Arbitrator, ADR Chambers

IN THE MATTER OF AN ARBITRATION IN RELATION TO THE POTATO PROCESSING CONTRACT NEGOTIATION ORDER

BETWEEN:

PRINCE EDWARD ISLAND POTATO BOARD

(the "Board")

- and -

McCAIN FOODS (CANADA)
a division of McCain Foods Limited

(the "Processor")

DECISION

THE ARBITRATION

1. I was appointed Arbitrator in this matter pursuant to Section 8(2) of the Potato Processing Contract Negotiation Order dated December 4, 2009 (the "Order"), the parties being unable to agree upon all the terms and conditions of a contract for use by the Processor in the purchase of Processing Potatoes for the 2013 crop year. The defined terms in this Decision have the same meaning as the defined terms in the Order.

2. A Procedural Hearing occurred by conference call on April 15 2013 and the parties agreed to a timetable for the exchange of submissions and their respective final offers and replies.

3. By conference call on April 23, 2013, the parties agreed that there would be no in- person hearing.

4. Section 4 of the Order provides that in making my decision, I am to take into account the factors outlined in Section 4 of the Order, namely:

(a) the prices or projected prices paid for potatoes by competing processors in competing markets areas;

(b) the quantity or projected quantity of potato production in Prince Edward Island and competing market areas;

(c) the average cost of production of potatoes produced for Processing purposes;

(d) prior contracts entered into by the Processor; and

(e) other factors which historically had been taken into consideration in arriving at contracts for the sale of potatoes for Processing Potatoes.

5. Section 8 of the Order requires that I select one of the offers of the parties in its entirety, without modification.

ISSUES FOR ARBITRATION

6. The Board proposes that the terms of the 2012 Grower Contract with the Processor be extended for the 2013 contract year, with no changes to the terms and conditions of the contract other than the removal of Exhibit A, the one year addendum which previously amounted to a price reduction of $0.10/cwt.

7. The Processor submits that to remain competitive in the North American marketplace and to avoid production cuts and job losses, it requires a price decrease of $0.50/cwt on the base price paid for the 2012 crop.

POSITIONS OF THE PARTIES:

8. **Board** – The Board submits that:

(a) An extended contract for the 2013 year with the removal of Exhibit A being the one year addendum which previously amounted to a reduction in price of $0.10/cwt offers sufficient balance for the Processor to remain competitive in the marketplace recognizing the profitability of the processing industry, the increase in cost of production estimates for the growers as well as contract agreements reached in other regions of North America.

(b) 2012 was a strong year for North American potato processors with steady increases in sales volume, prices and revenue margins.

(c) The processors historically have been able to implement market rate increases to offset cost input increases and North American Processors have experienced revenue improvement through an increase in the final price of the product.

(d) Historically, contract prices in Prince Edward Island have been consistent with changes in other regions which have shown increases in prices of 1.5% to 2.1% for the current year.

(e) Cost of production rose in the 2012 crop year and it is estimated there will be an increase in 2013 from $2,904 per acre to $2,978 per acre. Accordingly, there is no justification to decrease the price paid to growers with increasing production costs.

(f) The price gap paid to growers in Prince Edward Island and the Pacific Northwest is due to fundamental differences in processing potato production between various North American regions due to growing conditions and distance to the market. These differences result in a difference in return per acre of 15% in the Pacific Northwest and 6.4% in Prince Edward Island. If prices paid to growers were reduced by the amount requested by the Processor, the resulting return of $36 per acre would be an unsustainable level of return for growers in Prince Edward Island.

(g) The growers require that the current proposed contract (other than the removal of the one year addendum) be extended so that they can be economically sustainable. A reduction in price would leave the growers without funds to make necessary investments and improvements.

9. **Processor** – The Processor submits that:

(a) 64.4% of its production is exported around world.

(b) Its costs of transportation have increased due to fuel price increases which affect costs because of the large volumes shipped by truck by the Processor.

(c) The higher Canadian dollar affects competitiveness as competitors are importing into Canada. Increased competition has resulted in declining volumes. Customers are sourcing product from other regions due to lower costs. This has led to plant layoffs and reduced hours because of reduced demand. Without a price reduction, job losses and spin offs from factories in Prince Edward Island will continue and the Processor will be forced to make further productions cuts.

(d) Increased freight costs affect the Processor's model for distribution which depends on factories in North America strategically spread out geographically using trucks which until recently was the most competitive mode. Rail is now more widely used to move product from western factories to the eastern markets.

(e) Competing processors in the Pacific Northwest have an advantage over eastern processors because of lower costs of production leading to a 30.5% increase in the gap between contract prices in the two areas over the last 5 years. This has allowed the competition to add capacity with new plants and to increase their market share. The Processor seeks to narrow the price gap of $1.96 between the two areas so it can remain competitive in the marketplace particularly in the export market where the growth in the industry exists.

(f) Without a price reduction of $0.50/cwt on base price paid for the 2012 crop, the Processor's competitiveness in the market place will continue to erode.

DECISION AND REASONS

10. After careful consideration of the submissions of the parties, I select the final offer of the Board submitted on April 18, 2013 in its entirety without modification. That offer proposed that the 2012 Grower Contract with the Processor be extended for the 2013 contract year, with no changes to the terms and conditions of the contract other than the removal of Exhibit A. In my view, this offer is a fair and reasonable offer in all the circumstances.

11. In making my Decision, I have considered the factors outlined in Section 4 of the Order and I accept the submissions of the Board including:

(a) the contract price requested for the 2013 contract year is consistent with recent price increases in North America;

(b) the cost of production is increasing;

(c) there are fundamental differences in processing potato production between various North American growing regions, making it difficult to compare prices in the eastern region against the western region; and

(d) the proposed contract is a fair balance between the needs of the growers and the Processor.

Dated April 29, 2013.

Peter G. Cathcart, Q.C.
Arbitrator