



ONTARIO PORK

WHITE PAPER ON THE FINANCIAL PROTECTION PROGRAM

BACKGROUND:

In June 2009, Ontario Pork received the results of a Financial Protection Program (FPP) actuarial study from Towers Perrin indicating various options for possible implementation. The key findings of the actuarial study were:

- Preload the initial fund with an industry investment of \$3 million.
- Grow the fund to sustainable level of \$5 million over a 5 to 10 year period.
- Set premiums in range of 3 to 7.5 cents per market hog slaughtered to support the fund including costs associated with determining financial responsibility of license applicants and Financial Protection Board activities (The more you preload the fund, the lower the premium).
- Set program coverage at 100% (70 to 90% may be more prudent).
- Establish licensing provisions with strict rules for financial responsibility assessment.
- Set probability of ruin for the fund at 1 in 80 years.
- Establish a 5 day payment cycle from slaughter day (day 0).

Over the past ten years there have been only two small defaults in Ontario. However, in early 2009 there were defaults in the US, and a recent default by a livestock auction barn in Ontario underline that there is always a risk that producers may not receive payment for their animals.

Should a default occur under the parameters above, affected producers would claim against the fund and receive coverage based on a level set by regulation. The administrative licensing support and the Financial Protection Board functions could be tailored to capture synergies with similar activities occurring under the Beef Financial Protection Program. Based on the outcome of the pork industry consultations and further discussions with OMAFRA, any decisions made would ensure the availability of a robust and cost efficient administration of the program.

THE BEEF FINANCIAL PROTECTION PROGRAM:

The Ontario Beef Cattle Financial Protection Program (OBCFPP) lists 7 requirements for producers participating in that program.

1. Always deal with a licensed dealer. Don't risk selling to an unlicensed dealer. If there is any doubt, ask to see the license.
2. Ensure payment is made within 2 business days of sale. Day of sale can mean:
 - day of weighing where price is determined on a live weight basis;
 - day of grading where price is determined on a carcass grade basis; or
 - day of purchase where price is determined on a per head basis.
3. Ensure payment is received in a timely manner. If you receive payment:
 - by courier or electronic transfer, then you should receive payment no later than 3 business days
 - from the date of sale. If you do not receive payment in that length of time, the payment is late.
 - by mail, you should receive payment no later than 7-8 days from the date of sale. If you do not receive payment in that length of time, the payment is late.
4. Deposit the cheque within 5 banking days of receiving it.
5. Do not extend credit to the dealer. This means that you should never sell to the same dealer if the payment for a previous sale is late.
6. If a payment is not received on time, or if a cheque bounces, a producer must notify the OBCFPP Program Manager immediately.

7. If you are going to make a claim, you must apply within 30 days of when the payment was due.

If a similar program were offered for pork producers, points 2 and 7 appear to exclude a significant segment of Ontario hogs which are sold with a 7 – 11 day payment schedule.

PRODUCER CONSULTATIONS:

Producers discussed the possible development and estimated cost of a FPP at the November 2009 Policy Day on the estimated cost of a FPP for the hog industry. While most delegates supported the option of a FPP they were clear in not wanting to pay for it. In order to initiate the development of regulations necessary to create a FPP, OMAFRA requires that a broader consultation be undertaken by Ontario Pork to determine the level of producer support.

Under the Farm Products Marketing Act there is not the provision to create a reserve fund to strictly pay producers in the event of a default on a sale.

In June and July Ontario Pork hosted a survey on the need for an All Perils Mortality Insurance Program. In that survey 48% of producers said that under a government cost shared program they would definitely or probably purchase insurance coverage, while only 15% would probably not or definitely not purchase coverage. When asked about participating in a producer only program only 10% of producers would definitely or probably purchase coverage while 36% of producers would definitely not or probably not participate. While not directly addressing the question of a financial protection plan, the survey results do indicate that producers would rather keep their money in their own operations than participate in fully self- funded programs.

CURRENT SITUATION:

Until the implementation of the Minister's May 13 decision declaring that hogs will be marketed through an open market on or before Dec 4, 2010, Ontario Pork continues to protect Ontario producers in the marketplace through the use of three instruments. In addition to licensing all buyers of market hogs, Ontario Pork requires the testing for

financial responsibility or the deposit of a Letter of Credit (LC) assigned to Ontario Pork to cover the sale value in case of default occurring between the time hogs leave the farm and the payment is received. Those buyers are then limited to purchases matching the value of the LC provided. Finally, Ontario Pork has an accumulated pool of reserves that may be used to pay producers in the event of a default.

Ontario Pork has taken the issue of payment protection to the Hog Industry Advisory Committee to determine next steps in developing a Financial Protection Plan or an alternative to mitigate producer risk. In the absence of a FPP or regulation there won't be any payment protection for producers. If a FPP was agreed upon, it could take 18 months to develop and implement either of these options.

QUESTIONS FOR POLICY DAY DISCUSSION AND PRESENTATION:

We would request that each county association come to policy day prepared to present their answers to the following questions with the group:

1. Assuming no government funds were available to launch and maintain the program, do you feel there should be a Financial Protection Program?
2. Should Ontario Pork use producer funds to pre-load a program?
3. Is there a premium level (eg.minimum \$0.03/hog) where a program would be viewed as workable?
4. Should a pork Financial Protection Program be mandatory?