

SENATE

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**VALUE-ADDED
AGRICULTURE IN CANADA**

Report of the Standing Senate Committee
on Agriculture and Forestry

Chair

The Honourable Joyce Fairbairn, P.C.

Vice-Chair

The Honourable Leonard J. Gustafson

December 2004

MEMBERSHIP

The Honourable Joyce Fairbairn, P.C., *Chair*

The Honourable Leonard J. Gustafson, *Vice-Chair*

and

The Honourable Senators:

* Jacob Austin , P.C. (or William Rompkey, P.C.)

Catherine S. Callbeck

Aurélien Gill

Elizabeth Hubley

James F. Kelleher, P.C.

* Noël Kinsella (or Terry Stratton)

Terry M. Mercer

Donald H. Oliver

Pierrette Ringuette

Herbert O. Sparrow

David Tkachuk

* Ex-officio members

In addition, the Honourable Senators Chalifoux, Day, LaPierre, Lawson, St. Germain, P.C., Wiebe were members of the Committee at various times during this study or participated in its work.

Staff from the Parliamentary Research Branch of the Library of Parliament:

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Previous Committee Clerk involved with this study:

Keli Hogan

Line Gravel
Clerk of the Committee

ORDER OF REFERENCE

Extract from the *Journals of the Senate*, Tuesday, October 19, 2004:

The Honourable Senator Fairbairn, P.C. moved, seconded by the Honourable Senator Callbeck:

That the Standing Senate Committee on Agriculture and Forestry be authorized to examine the issues related to the development and marketing of value-added agricultural, agri-food and forest products, on the domestic and international markets;

That the papers and evidence received and taken on the subject during the Second and Third Sessions of the Thirty- seventh Parliament be referred to the Committee;

That the Committee submit its final report to the Senate no later than December 23, 2005, and that the Committee retain until January 31, 2006 all powers necessary to publicize its findings.

After debate,

The question being put on the motion, it was adopted.

Paul C. Bélisle
Clerk of the Senate

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FOREWORD

From September 2003 to May 2004, the Standing Senate Committee on Agriculture and Forestry held hearings in Ottawa to discuss issues related to the development of value-added agricultural and agri-food products and their marketing, both domestically and internationally during which Senator Donald Oliver presided as Chair of the Committee. The Committee is encouraged by the promise that value-added initiatives hold for the farming sector. The goal is to realize that promise by finding ways to assist farmers and remove the obstacles they face in pursuing value-added business strategies.

The Report is structured to reflect the views of the witnesses heard by the Committee during proceedings. The witnesses consisted of farm groups, agri-food trade representatives, farmer-owned cooperatives, cottage industry producers, the Internal Trade Secretariat and federal government officials from the National Farm Products Council, the Canadian Food Inspection Agency and Agriculture and Agri-Food Canada. The Committee held 13 meetings and sat for over 25 hours, hearing 33 witnesses. Canada's agricultural and agri-food sector is vital to this country's economy and society. In 2002, it accounted for over 8% of our total gross domestic product and employed roughly two million people, providing one in eight jobs. By encouraging the value-added component, we can help ensure that this sector remains central to Canada's future.

The Committee would like to recognize the excellent direction, input and commitment that the previous Chair of the Committee, Senator Donald Oliver, provided throughout this study. Also the Committee would like to recognize Senator Leonard J. Gustafson who held the Chair previous to Senator Donald Oliver for his equally dedicated efforts to this study.

LIST OF RECOMMENDATIONS

A. Food Safety

1. That the federal government expand the application of food safety systems such as the Hazard Analysis and Critical Control Points (HACCP) system among commodity sectors, and enhance funding to help small-scale food producers and processors achieve HACCP standards or other similar food safety and monitoring standards.

B. Quality Standards

2. That the federal government assist the wine industry in Atlantic Canada with funding for the development of a quality-assurance governance system in order to facilitate the implementation of national Vintners Quality Alliance standards.
3. That the costs associated with Canadian Food Inspection Agency food safety requirements that are put in place due to the adoption and enforcement of national wine standards be waived for the first two years of implementation for small wineries.

C. Organic Agriculture

4. That the federal government work with the organic sector throughout the value chain, and help establish an organic value-chain round table to address issues that restrict the production, distribution and retailing of organic agricultural products.
5. That the federal government provide leadership and work with the provinces and the organic industry to put in place national regulations specifically on the labelling of products of organic agriculture, no later than 2005.
6. That the federal government develop tax and expenditure incentive programs that recognize the extent to which organic practices benefit the environment, in order to help farmers make the transition to organic farming.
7. That the federal government commission a study to examine the Canadian Wheat Board's organic grain policy, with the goal of facilitating the marketing of Western organic wheat and barley.

D. Farmer-Owned Food Processing and Cooperatives

8. That the federal government investigate options such as loan guarantees and other measures that would increase access to capital for farmers considering the purchase of New Generation Cooperative shares.
9. That the Canadian Wheat Board allow further flexibility in developing New Generation Cooperatives in Western Canada.

E. Supply Management

10. That the federal government facilitate development and marketing of value-added agriculture within the supply management system by revisiting, with the industry, the system's regulations and terms.

F. Local Experience and Marketing

11. That the federal government introduce or increase marketing initiatives through the Canadian Agriculture and Food International program, and other programs, to aggressively promote high-quality Canadian products domestically and around the world.
12. That the federal government provide to all farmers national and international marketing seminars on a continuous basis.
13. Recommendation 13: That the federal government establish a "One Stop Web Center" that would communicate agricultural programs, research and other initiatives.

G. Research and Innovation

14. That the federal government increase funding for agricultural research and development in areas specific to the public interest, such as food health and safety, and the environment.
15. That the federal government adopt a comprehensive national research framework that considers broad agricultural research issues across commodity sectors.
16. That the federal government establish a cross-sector value-added round table focused on issues specific to agricultural research and innovation.

H. International Trade

17. That Canada's WTO negotiations identify, as one of Canada's priorities, the reduction of tariff rate escalation practices of setting higher tariffs on processed products.
18. That the federal government consult, and include in negotiations of trade implementation agreements, unbiased industry experts who have extensive knowledge of the processing and manufacturing requirements of the industry or industries that could be affected by these agreements.
19. That the federal government consider innovative ways to use the venture capital funding announced in the 2004 federal Budget to increase value-added capacity in the livestock and other agricultural sectors.

I. Interprovincial Trade

20. That the review called for in Article 902.4 of the Agreement on Internal Trade, with regard to the scope and coverage of agricultural internal trade, be tabled as per the Agreement.
21. That the comprehensive review called for in Article 903.2a of the Agreement on Internal Trade, with regard to the framework for governing supply management, be tabled as per the Agreement.
22. That a review of interprovincial marketing, distribution and access to points of sale of alcoholic beverages be conducted by federal and provincial governments under the auspices of the Agreement on Internal Trade.

INTRODUCTION

Value-added agriculture has attracted considerable attention in recent years as a means to increase and/or stabilize farm incomes and to rejuvenate primary agriculture and the rural economy. Value-added pursuits cover a wide range of business strategies and activities that enhance and extend beyond conventional farming and marketing of commodities. Examples include specialty crops, wine making, regional branding, cleaning and bagging grain, pasta processing, organic agriculture, service-embedded products and ready-to-eat convenience meals. For farmers, the attraction of value-added agriculture lies in the higher product premiums it generates and the fact that a greater portion of these accrue to the producer.

The move to value-added agriculture is fundamentally market-driven. Value-added activities are born from the necessity to adapt to the sweeping changes affecting the agriculture and agri-food industry. These changes stem from many interacting factors: the brisk expansion of agricultural trade, and the resulting concentration in the agri-food industry; an increasingly segmented consumer base; shifting consumer preferences; changing demographic and income profiles; innovation in food and non-food uses of agricultural products; and trade-related issues, including border closures, in an increasingly integrated global market.

This report briefly defines value-added agriculture, outlines factors influencing its growth, and reviews the benefits and opportunities it offers. It then discusses broad cross-sectoral categories that reflect value-added issues raised by witnesses: from food safety to marketing and on-farm processing to research and innovation. The remainder of the report highlights witnesses' concerns with respect to international and domestic trade.

DEFINING VALUE-ADDED

The term value-added can be interpreted in many ways.⁽¹⁾ In agricultural policy, it predominantly describes the steps that alter or add to a product or service. It is an innovation that enhances or improves (in the opinion of the consumer) an existing product, or introduces new products or new product uses. This allows the farmer to create new markets, or differentiate

(1) Value-added is often used in economics as a measure of output: the difference between the value of shipments and the cost of purchased inputs used in production. This concept is broader than the one used in the agricultural context, which usually describes product- or coordination-enhancing activities that lead to a higher portion of the consumer's food dollar accruing to the farmer.

a product from others and thus gain an advantage over competitors. In so doing, the farmer can ask a higher premium (price) or gain increased market share or access.

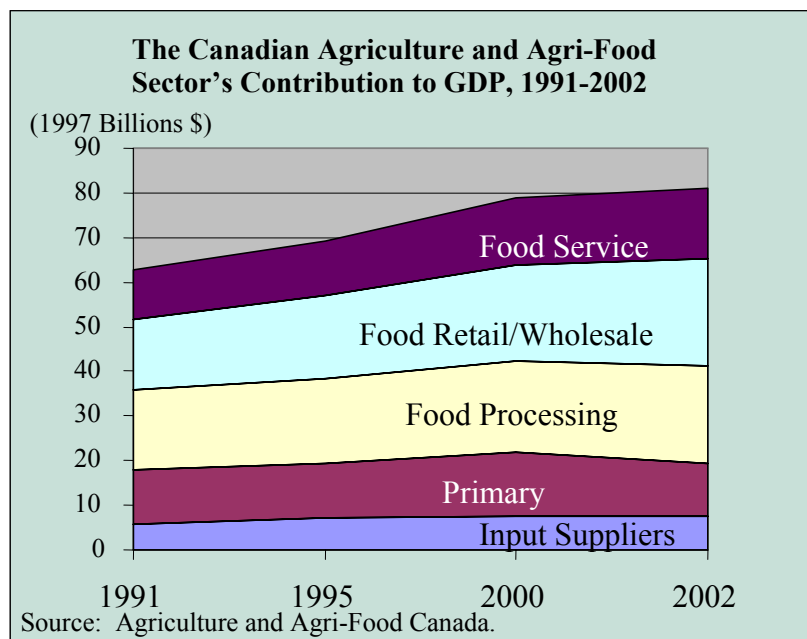
Vertical expansion of a farm operation through direct selling or a move to on-farm processing shortens the distance between farmer and consumer, and is often cited as a means to add value to the farm operation. Agricultural value-added can also involve new vertical and horizontal relationships that help increase profit margins, such as collective membership and investment in farm cooperatives. In addition, food quality chains can be protected or enhanced, and thus add value through partnerships along the food continuum from the farmer to the processor, distributor and retailer.

Adding value does not necessarily involve altering a product; it can be the adoption of new production or handling methods that increase a farmer’s capacity and reliability in meeting market demand. Value-added can be almost anything that enhances the dimensions of a business. The key is that the value-adding activity must increase or stabilize profit margins, and the output must appeal to the consumer.

AGRICULTURE AND MARKET FORCES

A. The Transformation of Agriculture in Canada

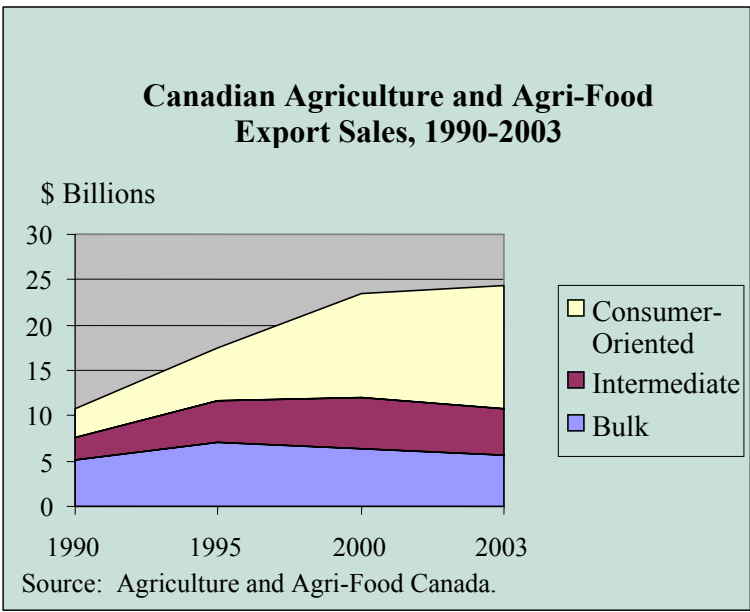
The Canadian agriculture and agri-food system has changed significantly over the last two decades. This transformation was spurred by changing consumer preferences, advances in technology and innovation, and multinational agreements such as the World Trade Organization (WTO) Uruguay Agreement on Agriculture, which brought agriculture to the forefront of trade negotiations and contributed to reductions and revisions of tariff protection and domestic support subsidies.



The transformation has been linked to the growth in the value-added or consumer-oriented sector. Value-added is the fastest-growing component of the agriculture and agri-food system. However, the industry as a whole is growing more slowly than the overall economy. While the domestic market is the key destination for value-added shipments, Canadian expenditure on food is among the lowest in the developed countries; and this increases the importance of international trade in agriculture and agri-food products.

Trade in bulk commodities is very competitive and price-sensitive. Lower-cost producers in other countries helped by lower production costs, higher yields or production subsidies have put downward pressure on world prices. This trend has prompted Canadian farmers to diversify, specialize in premium markets, or compete head-on by increasing their efficiency and the size of their farms.

In 2002, Canada was the fourth-largest agriculture and agri-food exporter in the world, and the fifth-largest agriculture and agri-food importer.⁽²⁾ The export value of Canada's bulk commodities in 2003 was roughly the same as in 1990. The growth in export sales of consumer-oriented products, however, has more than quadrupled since 1990.⁽³⁾ Consumer-oriented products now account for half of Canadian agriculture and agri-food exports. The significant increase in the value-added sector marks a profound transformation in agriculture.



During Committee hearings, Michael Presley, Director General of the Food Value Chain Bureau, Agriculture and Agri-Food Canada (AAFC), indicated that a high degree of rationalization and consolidation has occurred in the agri-food system.

(2) Agriculture and Agri-Food Canada, *An Overview of the Canadian Agriculture and Agri-Food System*, May 2004.

(3) *Ibid.*

Over the past 15 years, the industry has been marked by rationalization as companies closed older, smaller plants across the country. The industry has also seen marked consolidation as mergers and acquisitions significantly reduced the number of active companies, particularly the middle range of firms. Companies are now generally either large national players or small regionally-based players.

Michael Presley, Director General,
Food Value Chain Bureau,
Agriculture and Agri-Food Canada

Market power over the years has increasingly shifted to the retail end of the food value chain. The Committee was told that the top five retail companies account for 60% of the market in Canada, and that even further concentration is possible. The Committee is concerned about the level of concentration among retailers and the market power they yield.

Competition for shelf-space is fierce, and farmers typically wield little market power. This often leads to lower prices being offered for their products. Some food processors have joined farm producers in trying to survive on low profit margins. The Committee was told that these changes have important implications for primary producers, particularly with regard to how they develop value-added strategies. For example, producers could consider how specific attributes of a food, or of its production, might tie in with changing trends, attitudes and preferences of consumers.

B. Changes in Consumer Demand

Consumers' demand for food is linked to factors such as population growth, demographic profiles, changing household structure, changing consumer values, disposable income and growth of the economy. The Committee heard testimony from AAFC stating that the growth in domestic market demand for food is roughly 2-3 % per year on a value basis. This growth rate is low, compared to the 1960s and 1970s. Canada's aging population and slower growth in disposable income are contributing to a slowdown in the growth in expenditures on food as a percentage of total expenditures. Moreover, the growth in food consumption is closely linked to population growth, which currently stands at roughly 1% annually. These factors make the food industry very competitive.

Not only is the food industry highly competitive, it is increasingly segmented. Many consumers want ready-made convenience food, which tends to increase the distance between the producer and the consumer and thus further reduce the farmer's share of consumer expenditures on food. On the other hand, new food value chains are creating value-added opportunities at the farm level. There is a growing demand for specialty products, notably those that appeal to health-conscious, lifestyle-conscious or non-traditional ethnic consumers.

Furthermore, consumers are becoming more aware of the production processes that go into their food. They are influenced by the origins of their food, how it is grown, processed and prepared. The Committee was told that surveys indicate that food purchasers rate food safety as their first consideration when choosing a food supplier.

Our surveys indicate that buyers are increasingly focusing on environmentally sensitive production practices, animal welfare standards and the ability of suppliers to supply organic products or non-genetically-engineered products.

Michael Presley, Director General,
Food Value Chain Bureau,
Agriculture and Agri-Food Canada

VALUE-ADDED AND THE FARM

A. Benefits of Value-Added

Value-added on the farm is born out of a necessity to adapt to a changing environment. It is market-driven and encompasses a vast range of activities designed to increase farm income and profit margins in a highly competitive, risky and segmented market. The notion of adding value on the farm has received considerable attention in recent years because it is seen as a way to rejuvenate the primary agricultural sector and provide a means of adapting to the various forces affecting agriculture. The strong social and economic importance of farming activities within the rural economy increases the significance of value-added agricultural initiatives, because the benefits spill over beyond the farm. Value-added agriculture is seen as a way to:

- increase employment and revitalize rural communities;
- reduce the economic risk associated with trade activities;

- diversify the economic base of rural communities;
- increase farmers' financial stability;
- promote a culture of research and innovation;
- reduce dependency on the world price of commodities;
- increase opportunities for smaller farms and companies through the development of niche markets;
- increase quality and brand recognition of regional and Canadian products;
- promote collective solutions and partnerships along the food value chain;
- help retain young farmers.

Current federal government efforts to promote value-added include a wide range of programs and services that fall under the Agricultural Policy Framework (APF) and other initiatives that provide research, financial assistance, feasibility studies, statistical data and advice to farmers considering value-added ventures. Key initiatives are the following:

- The Advancing Canadian Agriculture and Agri-Food (ACAAF) program⁽⁴⁾ supports projects that test or pilot value-added approaches and solutions; commercializes research results; and gathers, analyzes and shares information.
- Planning and Assessment for Value-added Enterprises (PAVE) that assist producers in developing business plans for value-added projects.
- Farm Credit Canada Ventures (FCCV) provides financing to develop value-added businesses and promote diversification in the agriculture and agri-food sector. In the 2004 Budget, the federal government committed an additional \$20 million to FCCV.

The Committee is concerned, however, that the federal government's emphasis is moving from farmed-based value-added programs to programs that focus on the processing and manufacturing sector without a tie-in to the farmer. The Committee believes that producer-driven value-added business ventures should be the principal focus of federal agricultural value-added programs.

(4) AAFC, News Release, "New Federal Funding Program Will Advance Agriculture and Agri-Food Industry," 7 April 2004. The ACAA program replaced the Canadian Adaptation and Rural Development Program (CARD).

B. Food Safety and Quality

Food safety and quality standards are core attributes of agriculture, and they are central to the federal-provincial-territorial Agricultural Policy Framework. Verifiable measures, such as food tracking systems and standards help position Canadian food products as safe, reliable and of a high quality. These measures help identify and respond to food safety issues, and thereby increase financial stability and help improve market access and value-added opportunities.

1. Food Safety

Value-added begins with food safety. In an environment where consumers are more knowledgeable and discerning about their food purchases, on-farm food safety systems and informing consumers about these systems can serve as a first step in increasing value for the farmer and for the industry.

Producers can position their products to cater to the discerning consumer and attract premiums through niche markets. These opportunities lie in meeting and exceeding the regulatory standards that ensure Canada's reputation as a safe and high-quality food producer. The public sector plays an essential role in initiating and enforcing a regulatory environment and officially recognizing standards that safeguard and promote trust in the agri-food system.

During proceedings, the Committee heard testimony indicating that surveys place food safety as food purchasers' highest consideration. Food safety has been at the forefront of media attention due to the economic fallout that followed the discovery of a single case of BSE in Alberta in May 2003 and the recent cull of British Columbia poultry and other birds as result of measures to contain the H7 avian influenza virus. There is a growing emphasis on tracking and tracing systems along a rapidly expanding agri-food continuum. Food is now shipped over great distances, fast and efficiently – offering a wider choice to consumers, but also expanding the potential impact of infectious agents or food-borne illnesses, particularly when production and processing have become more complex. This has led to the growing importance of food safety systems in order to help prevent, identify and remedy food safety problems. Tracking and tracing systems and identity preservation are features that can add value to products, since it reduces risk and contributes to product value.

Canadians trust the safety of their food. As noted by Michael Presley, one of the lessons of the BSE crisis was that Canadian consumers continue to regard Canadian beef as a

safe and high-quality product. This was made clear when Canadians increased their consumption of domestic beef during the months following the BSE discovery in May 2003. The Committee agrees that domestic confidence in the food system is highly important, particularly if access to export markets becomes restricted. However, the government must ensure that this trust is maintained.

One of the biggest challenges that we do face is that the biggest percentage of our operations is small, hobby operations with little to invest in their quality control programs. You can have the biggest, shiniest maple syrup producers making high quality syrup. Yet if one has a product that goes to class-one recall, advertised all over the newspapers and television, the entire industry suffers because people's perception of maple syrup as a safe product would be hurt.

Mark Wheeler, Member of the Board of Directors,
Ontario Maple Syrup Producers Association

The Committee was told that internationally recognized food safety based systems such as Hazard Analysis and Critical Control Points (HACCP), a control and monitoring system implemented by industry, was invaluable in the ongoing effort to re-establish international trade in the beef industry. HACCP complements existing food inspection programs, and helps to prevent and correct problems on the farm and at each step along the manufacturing process. The federal government, in partnership with commodity associations, funds programs that increase awareness and promote on-farm food safety and quality-assurance initiatives.

The Committee is concerned, however, at the cost of meeting regulatory standards and the capital costs facing many new, smaller-scale entrepreneurs who rely on small, value-added niche markets, or farmers expanding into food processing.

At this point HACCP is out of the reach of pretty well every maple syrup producer that I know of in respect of the cost for the program and the size of our maple syrup industry.

Mark Wheeler, Member of the Board of Directors,
Ontario Maple Syrup Producers Association

Recommendation 1: That the federal government expand the application of food safety systems such as the Hazard Analysis and Critical Control Points (HACCP) system among commodity sectors, and enhance funding to help small-scale food producers and processors achieve HACCP standards or other similar food safety and monitoring standards.

2. Quality Standards

Quality standards serve to recognize production practices and procedures that are differentiated, on the basis of quality and services, from other products. The products are identified through certification, labelling and branding. Quality standards make up part of a marketing strategy that informs the consumer and attracts premiums. The generic nature of primary agricultural products often leads to product differentiation that is based solely on price. Quality standards add value to a product and expand the marketing options for it.

Quality standards are generally voluntary, in that they exceed what is required for food safety standards. They may be established by a single farming business or be adopted industry-wide. They are essential in expanding an existing food value chain:

[T]oo often in Canada – and in horticulture in particular – we have supply chains but we do not have value chains. In other words, we have well-defined relationships between buyers and suppliers down to the primary commodities but we do not see a shared value premise throughout the whole chain.

Michael Presley, Director General,
Food Value Chain Bureau,
Agriculture and Agri-Food Canada

Quality standards are an important step in developing premium categories in food products. They help position Canadian products in elite markets. They enhance Canada's reputation in export markets, from which benefits can spill over across the Canadian agri-food sector. They also develop a sense of national pride in the purchase of domestic products.

Quality standards are usually grounded in provincial or federal legislation that provides protection from false quality claims and mislabelling. The Committee was told that the federal government is working with the food industry and the CFIA on issues related to the cost and enforceability of quality standards.

The Standards Council of Canada oversees Canada's national standards system and accredits organizations such as the Canadian General Standards Board (CGSB) that develop standards in Canada. The accreditation programs are based on internationally recognized guides and standards. The CGSB facilitated the development of national standards for the voluntary

labelling and advertising of foods that are, and are not, products of genetic engineering, and the national voluntary standard for organic agriculture.

The development of national quality standards clarifies choices for consumers and fosters consistency and confidence in Canadian products. Appropriate national standards and the development of national regulations are imperative in maintaining and increasing export markets in organic agriculture (for details, see the section on organic agriculture, below). Further, Don Dodds, Chair of the Ontario Maple Syrup Producers Association's Research and Technology Committee, emphasized the need for uniformity in grading among maple syrup regions in North America, in order to reduce confusion in trade overseas. It is recognized that North American uniformity in maple syrup quality standards may be difficult to accomplish, but the first step is to have Canada's four maple syrup-producing provinces work closely together to discuss mutually beneficial marketing and branding strategies.

a. Quality Standards and the Wine Industry

In the 1970s, Canadian wines were generally produced from low-quality grapes and carried a stigma of being of lesser quality. The industry was protected by preferential tax treatments. In 1989, following the Canada-United States Free Trade Agreement and a General Agreement on Tariffs and Trade (GATT) panel ruling, the preferential tax treatments were eliminated, forcing the wine industry to adapt to a new competitive environment. A strategy was implemented to position Canadian wines as a premium product. The cultivation of higher-quality grapes helped Canadian wineries move to premium markets. Wineries adopted an industry quality standard: Vintners Quality Alliance (VQA). The VQA imposed stringent production, labelling and quality standards similar to those adopted in France, Italy and Germany; for example, VQA wines are made entirely from Canadian grapes and are subjected to a tasting panel. Over time, the quality of Canadian wines was transformed, and Canadian VQA wines are now acclaimed domestically and abroad as high-quality wines.

VQA standards are implemented in two regions of Canada: Ontario and British Columbia. In both provinces, the standards are enforced through provincial regulation. The Committee heard testimony that the federal government and the wine industry are working to adopt a national standard with federal regulation. In its submission to the Committee, the Canadian Vintners Association (CVA) informed the Committee that the primary reason for establishing a national wine standard is to give Canada a credible national appellation of origin

system for quality wines. The Committee was informed that difficulties, such as with the effective enforceability of a national standard, have so far prevented its establishment.

The Committee was told that the proposed national standard had provisions to accommodate wineries that could not afford to invest in the quality-assurance requirements necessary to meet the full VQA standard. These provisions are of interest to small wineries, and to wineries in other wine-producing regions such as Quebec and Nova Scotia. To this end, the national standard would include three tiers of accreditation representing different VQA quality levels. The Committee was informed, however, that Atlantic Canada does not have a quality-assurance governance system in place to implement tiered VQA standards.

Recommendation 2: That the federal government assist the wine industry in Atlantic Canada with funding for the development of a quality-assurance governance system in order to facilitate the implementation of national Vintners Quality Alliance standards.

In order to adopt national wine standards, the industry would have to meet requirements under the *Canadian Agriculture Products Act* (CAP). The Committee was informed that, since the CFIA would regulate standards under the CAP Act, the wine industry would have to meet additional CFIA food safety requirements. This had not previously been a requirement, because wine is not conducive to bacterial contamination due to its acid and alcohol content. The CVA is concerned that the initial registration costs and ongoing inspection costs required by the CFIA would be particularly onerous for smaller wineries. The CVA proposes that the CFIA commit to waive these fees for the initial years of implementation.

Recommendation 3: That the costs associated with Canadian Food Inspection Agency food safety requirements that are put in place due to the adoption and enforcement of national wine standards be waived for the first two years of implementation for small wineries.

C. Organic Agriculture

Organic agriculture is a form of value-added agriculture. It is a small but growing market, and it extends across the agriculture and agri-food system. In general, organic foods are

The Canadian Organic Growers association defines organic agriculture as a holistic system of production designed to both optimize productivity and encourage diversity in communities within the agro eco system including soil organisms, plants and people.

more costly to produce, more difficult to produce in large volumes and, for most crops, the production suffers from reduced yields. However, its economic attraction lies in the higher premiums it generates by appealing to a growing consumer concern about the environment, food safety, nutrition and awareness of agricultural production systems.

The wellness issue is based and translated into an interest in buying organic products. It is not necessarily proven that the organic products are more safe and healthy, but there is a belief that they might be healthier to consume. Therefore, you will see premiums attached to that product.

Michael Presley, Director General,
Food Value Chain Bureau,
Agriculture and Agri-Food Canada

The Committee was told that the organic sector appears to be growing out of its niche market category. Multinational corporations are investing in organic food product lines, and mainstream supermarkets are committing lucrative shelf-space to organic products.

The Committee heard testimony indicating that global sales of organic agricultural products are roughly \$23 billion annually. The level of Canadian consumption of organic foods is only 1-2% of total food consumption, but it is growing at a rate of 20% per year – an impressive increase in a food industry that is growing 2-3% overall.

However, the Committee was presented with figures indicating that the growth in certified organic farms in Canada has flattened in recent years. This is a matter of concern, since the domestic demand for organic products shows considerable strength – and this demand is increasingly being met by imports, mainly from the United States. The situation is especially unfortunate given Canada's conduciveness to organic farming practices, due to its fertile and varied land base, as well as a cooler climate that reduces the effects of pest and disease.

A huge gap is developing, and that gap is being met by foreign imports. That does very little for the Canadian economy. We are hoping that we can increase the number of Canadian producers who are farming under organic systems.

Laura Telford, Executive Director,
Canadian Organic Growers

The Committee heard from witnesses from the Canadian Organic Growers (COG) who suggested that a number of factors may be responsible for the diminishing growth of certified organic farms:

- Avoidance of the word “organic” in government policies, budgets and communications creates a perception of a marginal, unsuccessful industry.
- Organic production results in lower yields than conventional agriculture (although this may be due only to transitional issues).
- Farmers may not have confidence in the sustainability of the premium prices associated with organic agriculture.
- Farmers do not have time to learn or perform new farming techniques and practices that are labour-intensive.
- Governments’ withdrawal from extension services leaves private-sector suppliers to provide technical knowledge to farmers. Since suppliers of organic farmers are usually smaller and do not have the resources to supply technical support, most of the gap created from the government withdrawal from extension services are being met by large non-organic farm input suppliers as an enticement to purchase their products.
- The current system of mono-crops, supply management and Canadian Wheat Board (CWB) policies do not favour organic agriculture.
- There is a lack of federal regulations specifically on the labelling of organic agricultural products.

The Committee recognizes the benefit of industry-specific value-chain round tables that have been established to create a venue for producers, processors, distributors, retailers and others, along with provincial and federal governments, to work out strategies to succeed domestically and in export markets. Round tables have been established for major commodity groups, such as beef and pork. The Committee believes that the rapidly growing organic agriculture sector is set apart from other sectors due to its strong reliance on a trace-back system and because production practices and problems facing organic agriculture are not properly addressed by existing industry value-chain round tables. Therefore, the Committee recommends:

Recommendation 4: That the federal government work with the organic sector throughout the value chain, and help establish an organic value-chain

round table to address issues that restrict the production, distribution and retailing of organic agricultural products.

While a national standard for organic agriculture is in place, there are currently no national⁽⁵⁾ regulations specific to the labelling of organic agricultural products. The system is voluntary, which means that it is not mandatory for a product to be certified before it can be sold as an organic product.⁽⁶⁾ This situation creates problems for exporters. In absence of a Canadian regulatory system that could be recognized by importing countries, Canadian exporters of organic products must be accredited by regulatory authorities in the importing countries. It is possible that trade in organic products may be interrupted if Canada does not adopt a national and mandatory regulated standard.⁽⁷⁾

We in the sector have been working toward a clear, effective regulation that is practical and affordable to implement. We must have a regulation in place as soon as possible in time to negotiate organic equivalents with the other countries with which we engage in trade.

We hope to see no interruption to current organic trade that is in place, and we hope to see improved opportunities to capture emerging markets in organic consumption for our farm families in Canada.

Janine Gibson, President,
Canadian Organic Growers

In order to ensure that farmers and other agri-food businesses are not dissuaded from entering the organic industry by the absence of national regulations on organic labelling, and to protect the integrity of the Canadian organic industry and prevent the loss of current and emerging export markets, the Committee recommends:

Recommendation 5: That the federal government provide leadership and work with the provinces and the organic industry to put in place national

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- (5) Quebec has organic regulations and a mandatory certification system.
 - (6) Currently, the mislabelling of products (including the mislabelling of foods as organic) is subject to action by the CFIA under the authority of the *Food and Drugs Act* and the *Consumer Packaging and Labelling Act*.
 - (7) The European Union, one the biggest markets for organic products, requires that the exporting country have a regulated national standard that is deemed EU-equivalent.

regulations specifically on the labelling of products of organic agriculture, no later than 2005.

The production practices and techniques of organic agriculture are founded on sensitivity to the environment. Society benefits in that such production practices benefit the ecosystem and the health of the environment surrounding the farm and beyond. The social benefit (or “positive economic externality”), however, may not be fully reflected in the price of organic products – a fact that may discourage some farmers from making the transition from conventional to organic farming. Therefore, the Committee recommends:

Recommendation 6: That the federal government develop tax and expenditure incentive programs that recognize the extent to which organic practices benefit the environment, in order to help farmers make the transition to organic farming.

In Committee proceedings, COG expressed its frustration with CWB’s Producer Direct Sale program, commonly referred to as the “Buy back” program. The program was designed to provide more marketing options to farmers. The program permits grain producers to market their own grain but requires the farmer to pay the difference between the conventional cash market price and the pooled price for their grain. Since price premiums are associated with organic grains, many organic farmers participate in this program. However, it is felt that CWB’s Producer Direct Sale program needs to be more flexible in addressing the unique needs and circumstances of organic farmers while not compromising the advantages afforded to Western grain farmers from the single desk marketer.

Buy-back systems through the Wheat Board have been a great challenge to many organic grain producers. We need to continually modify that system so that the benefits that some farm families have enjoyed through the Wheat Board are not compromised but those marketing independently and marketing a unique crop like organic are not penalized.

Janine Gibson, President,
Canadian Organic Growers

Recommendation 7: That the federal government commission a study to examine the Canadian Wheat Board's organic grain policy, with the goal of facilitating the marketing of Western organic wheat and barley.

D. Farmer-Owned Food Processing and Cooperatives

On-farm food processing is a vertical expansion of farm activities that serves to transform and enhance the appeal of the farmed commodity. Food processing can be as simple as washing vegetables or as complicated as processing ethanol. In any case, the move to food processing requires a shift in marketing practices. The benefit is that the farmer turned processor can benefit from being the supplier of his or her processing enterprise. On-farm processing also serves to diversify farm income and spread business risk.

However, the move from conventional farming practices to on-farm processing can be a risky transition:

Unfortunately, other efforts to move up the value-chain by individual farmers and groups of farmers have not always been as successful. Some of these ventures have been under-capitalized or lacked experienced management skills, while others were simply caught up in changing market or financial conditions which they could not overcome. Although some of the ventures have survived after restructuring the restructuring has sometimes meant the loss of control or equity of the original founder.

Michael Presley, Director General,
Food Value Chain Bureau,
Agriculture and Agri-Food Canada

The processing business is an entirely different enterprise than farming. It may involve different municipal/rural land-use and planning considerations, food processing

regulations and licences, food safety and inspection regulations, waste management plans, labelling and marketing strategies that are unfamiliar to the conventional farmer. These factors have led some farmers to form strategic alliances with large processing corporations in order to access inputs as well as distribution, marketing and knowledge services as a way to spread risk and generate value-added benefits. Also, the high level of capital needed for the transition to processing and manufacturing of food products have led other farmers to, form partnerships and cooperatives to spread the risk and achieve the critical mass necessary for larger ventures to be profitable. The Committee supports all types of viable financial arrangements that serve to reduce risk and increase, in the long term, income stability for farmers.

1. Cooperatives

Farm cooperatives are the second most prevalent type of cooperatives in Canada. (The largest are financial cooperatives, such as credit unions.) Farm cooperatives are a form of organization owned and controlled by a voting membership where members are usually responsible for supplying inputs (agricultural products) to the organization. Farmers have traditionally relied upon cooperatives to reduce uncertainty and overcome the lack of market power associated with producing generic commodities. Cooperatives can give farmers more bargaining power over inputs and value of outputs; they can reduce costs through economies of scale and provide greater market access.

The Committee believes that providing information to farmers on how to develop cooperatives is vitally important. The Committee supports the work of the federal Co-operatives Secretariat, which funds advisory services that help producers form cooperatives and find markets for their products. During proceedings, the Committee was made aware of new programs such as the Cooperative Development Initiative (CDI), which focuses on agricultural value-added as one of its six program priorities.

Farmer-owned cooperatives are designed to add value to farm output. In many cases, cooperatives form partnerships with processors in order to reach more lucrative markets. For example, the Committee was told how some herb and spice farmers who have low-volume crops have worked as a collective to guarantee quality and supply in order to facilitate access to markets for medication and food supplements. Most farmers' markets across Canada are cooperatives, and this is often the first step in gaining retail access for farm products.

2. New Generation Cooperatives

A focus on increasing value-added on the farm has contributed to the emergence of a new type of cooperative: New Generation Cooperatives (NGCs), or a closed cooperative. The structure of NGCs varies, but in most cases they are designed to add value for the farmer by giving farmers a stake in the processing and manufacturing of farm commodities. An NGC's membership comes with a contractual right and obligation to deliver a certain quantity and quality of farm input at a contracted price. Profits are distributed to members in proportion to the raw products delivered.

A business that involves processing raw materials often faces challenges very different from those facing farming enterprises. However, the farmers, as owners of an NGC, can hire managers to run the cooperative. Farmers thus reap the benefits of moving up the food value chain while continuing to do what they know and do best.

The Committee heard testimony from the Atlantic Beef Producers Co-operative (ABPC), an NGC controlled by independent Maritime cattle producers. ABPC are establishing a “kill cut” plant in Prince Edward Island in partnership with Co-op Atlantic, a Maritime retailer. ABPC and Co-op Atlantic are working together across the three Maritime provinces to supply Maritime-branded beef, which is already established as “Atlantic Tender Beef Classic” in the grocery stores of Atlantic Canada.

One of the things that we liked about the idea of building a plant together with a retailer was that it brought us into the marketplace. Before, as producers, we merely sold a commodity to a packing plant that in turn sold it to someone else down the chain. We felt that it was better for us to be involved in the chain as much as possible.

Dean Baglolle, Chairman,
Atlantic Beef Producers Co-operative

The Committee applauds ABPC's initiatives, which are an excellent example of regional producers working together to move up the value chain. Moreover, ABPC can take advantage of its size and unique circumstances to establish a branded plant with the flexibility to meet consumers' needs by offering full traceability, or by specifying feed requirements to member producers so that the product is of a consistent quality. By partnering with a retailer,

ABPC ensures that the product is guaranteed adequate shelf-space – access to shelf-space being often the most difficult obstacle facing new agricultural products.

The Committee also heard testimony from Prairie Pasta Producers (PPP), an NGC of Western Prairie durum wheat farmers. The PPP’s mission, as told to the Committee, was to form and operate an international durum processing plant, owned by farmers, with the goal of revitalizing their rural communities. During proceedings, Perry Mackenzie, Chairman of the PPP, informed the Committee that Canadian laws for incorporating NGCs resemble those of the United States, except that farmers in the United States are eligible for low-interest loans backed by the government on the purchase of NGC shares. This arrangement helps farmers who have little income to raise the often-significant capital needed to form and join an NGC.

Recommendation 8: That the federal government investigate options such as loan guarantees and other measures that would increase access to capital for farmers considering the purchase of New Generation Cooperatives shares.

The Committee heard testimony from the CWB indicating that the Board strikes a balance between setting a price that is conducive to value-added processing and a price that will optimize the farmer’s returns, and that the CWB supports value-added because it increases the demand for grain. The CWB cited arguments that its operations make Canadian milling and malting industries competitive by having a pricing mechanism that is transparent, fair and stable.

While it is true that these industries have grown significantly in Canada compared to the United States, the Committee is concerned about the difficulties that the CWB may pose for pasta-processing ventures. In testimony presented to the Committee, the PPP argued that the CWB would not exempt it from paying a price for grain that includes transportation fees, even though the PPP proposed to process its own grain and may not use those elevators. The Committee was told that the CWB could not accept various suggestions made by the PPP, such as allowing a separate pooling account for NGCs or allowing the PPP to use a small mill exemption.

The CWB’s position is that these proposals would have awarded the PPP an unfair price advantage over other grain farmers. In return, the CWB introduced policies such as stock-switching whereby farmers situated at a great distance from an NGC can become full cooperative members without incurring prohibitively high transportation costs. This arrangement broadens the pool of potential NGC investors.

To the extent that the CWB's single-desk marketing operations and technical assistance and services provide higher returns for grain farmers, they capture larger values for farmers. However, the Committee believes that the CWB can do more to encourage investment in value-added agriculture, particularly through farmer-owned processing initiatives. It is vital for the future of our rural communities that Canada consider options that either broaden the appeal of raw products through value-added business strategies or encourage value-added processing.

Recommendation 9: That the Canadian Wheat Board allow further flexibility in developing New Generation Cooperatives in Western Canada.

E. Supply Management

In Canada, poultry, egg and dairy industries operate under a national supply management system that is administered through federal and provincial legislation and agreements. The agreements differ for each commodity, but generally the system is managed by national marketing agencies in consultation with provincial marketing boards. The board of directors for each national agency is controlled by producers, but it also has representation from processors and other stakeholders. The provincial marketing boards negotiate commodity prices and volumes with processors. The federal National Farm Products Council (NFPC) oversees and reviews the operations of the national supply management system.

Supply management provides more bargaining power to primary producers. Principally, it regulates supply by restricting production and marketing through quotas, and this in turn increases prices. A supply management system also directly sets the price of the commodity. The domestic market is protected from lower-priced imports through a system of tariffs and quotas.

Supply management offers several evident benefits to farmers. It enables farmers to capture a larger portion of the consumer dollar; it also provides price stability. There are, however, some drawbacks. For example, because farmers operating under a supply management system receive protected returns for their products, they may have less incentive to seek value-added ventures. Also, there is a concern that supply management greatly increases the costs for new entrants, since production quotas may be difficult to obtain and priced out of reach for most new smaller farm operations.

Therefore, as in any sort of regulated industry, obstacles do exist. The marketing agencies are trying to view these as challenges and see how they can adapt their systems so that the obstacles are removed and farmers can gain advantage in value-added production.

Cynthia Currie, Chairperson,
National Farm Products Council

The Committee recognizes that the supply management system has adopted more flexible policies and has fostered dialogue with stakeholders with respect to value-added strategies, particularly for producer-owned cooperatives and in some cases within the organic sector.

The Committee feels, however, that more must be done to encourage value-added business ventures. During Committee proceedings, a representative from the COG expressed concern that supply management, as it is currently structured, hinders the entry of new organic farmers. The Committee heard testimony that 54% of organic farms in Canada earn less than \$50,000 in gross annual sales. Most organic farmers and other small farm operations catering to niche markets simply cannot survive at their current scale of operation if they are required to purchase expensive quotas.

Recommendation 10: That the federal government facilitate the development and marketing of value-added agriculture within the supply management system by revisiting, with the industry, the system's regulations and terms.

In recent WTO negotiations in Geneva, a trade framework emerged that did not include items that proposed reductions in over-quota tariffs, which currently protect supply managed sectors from lower priced imports. Nevertheless, there is an overriding concern that future WTO negotiations will involve market access issues that may put pressure on cutting tariffs that protect supply managed products. The Committee is concerned that Canadian producers under supply management may not be prepared for the potential reduction in tariff barriers. The Committee supports the efforts of the federal government in vigorously defending Canada's supply management system in WTO negotiations. However, the Committee recognizes the need to help producers, who have made substantial investments in the system, to

adjust to the new trade arrangements if, indeed, the WTO framework leads to reductions in tariff barriers. Farm-based value-added programs should be part of the long-term transitional strategy.

F. Local Experience and Marketing

1. Direct Selling and Agri-tourism

Farmers can increase their profit margins by selling directly to consumers, without recourse to a distributor. In order to do this effectively, farmers must align products and services to buyer preferences. It is recognized that producers' success in adopting direct selling strategies varies across the country, depending largely on market proximity. However, tools such as the Internet can provide innovative options for farmers wishing to expand into niche markets. E-commerce can be a cost-effective tool to inform buyers and to market directly to stores, restaurants and the consumer.

Increasing numbers of consumers are looking for authentic farm and food experiences. More and more people are planning their leisure activities around agri-tourist attractions, including pick-your-own farms, bed-and-breakfast farm accommodations, farmers' markets, fairs, festivals, roadside markets, maple sugar shacks, wine tours and seminars.

The new consumer...is motivated by a very different quest – the quest for authenticity. The added value they seek is in authentic products. They look for products that are natural, located in a specific time and place, and they will, if the experience is intriguing enough, travel to bear witness to that authenticity.

Linda Bramble, Industry Liaison,
Cool Climate Oenology and Viticulture Institute,
Brock University

Agri-tourism is an expansion of the food experience. A visiting consumer is often looking for diversion, education, or active involvement in farm activities. Agri-tourism also serves to link urban consumers to Canada's rural communities, which are rich in heritage and central to our nation's identity. It is thus a means to revitalize our rural communities.

2. Marketing and Regional Branding

Regional branding is a powerful marketing tool. It can be used to highlight the distinctive taste and quality of particular food products by linking them to unique attributes of a

region, including its cultural heritage or landscape. Regional branding gives an added identity to a product, which farmers can use to differentiate it from competitors' products. It provides information to consumers who like to make a point of buying locally or regionally. It promotes product recognition and consumer loyalty, and is another means to link the farm gate to the consumer plate. Regional branding is also linked to quality standards.

We believe very strongly in the gate-to-plate concept, whereby we will be able to offer [a] product that consumers in the Maritimes and Atlantic Canada know is locally raised. They know the producers who helped to put it there. The stores can also take pride in knowing that it is a locally raised product.

Dean Baglole, Chairman,
Atlantic Beef Producers Co-operative

Attributes such as food health and safety, quality standards and environmentally sustainable practices are an important component of a national, as well as regional, branding formula. It should be noted, however, that it takes persistent marketing efforts and funds to attract "Made in Canada" premium-label recognition beyond our borders. The federal government funds the Canadian Agriculture and Food International (CAFI) program, which provides matching funding to groups in the agriculture and food exporting industry. The CAFI program helps develop markets by promoting the Canada brand around the world as superior in safety and quality, and in consistency in meeting market demands. The CAFI program also funds industry-led trade advocacy efforts to promote and defend Canada's interests in world trade.

Nevertheless, the Committee heard from numerous witnesses about the need to increase the marketing of "Made in Canada" products within and beyond our borders. The Committee is concerned that many Canadian consumers are often not aware of the origins of the food products they purchase. The Committee is impressed with the marketing strategy implemented by Nova Scotia, "Taste of Nova Scotia," which brings together quality food products from all parts of the province ranging from agricultural businesses, wineries, breweries, chocolate makers, meat and fish processors, jam and maple syrup producers and baked goods. The program takes advantage of the culture and history of the region to accentuate the uniqueness and quality features of its premium products. The Committee believes that such a

program should be used on a national scale and vigorously promoted around the world. The Canadian food industry as a whole is served by the promotion of our premium products.

Recommendation 11: That the federal government introduce or increase marketing initiatives through the Canadian Agriculture and Food International program, and other programs, to aggressively promote high-quality Canadian products domestically and around the world.

The Committee is concerned that not enough is being done to provide farmers the necessary information and services needed to innovatively market their products.

Recommendation 12: That the federal government provide to all farmers national and international seminars on a continuous basis.

Recommendation 13: That the federal government establish a “One Stop Web Center” that would communicate agricultural programs, research and other initiatives.

G. Research and Innovation

Research fuels the development of innovative technologies, techniques and practices that improve quality and extend utilization. New technologies and farming practices have substantially increased farm productivity over the last 50 years. Research can also expand the sphere of value-added possibilities. The emergence of new commodities and new applications of existing commodities are made possible through research. It is at the forefront of efforts to initiate new crops or livestock systems, and it can assist in health and safety fields as well as environmental protection strategies. Research can also lead to innovations in coordination and agri-food management strategies that enhance a product’s reliability and capacity to meet highly variable market demands, and thereby add marketable value to the product.

Advances in science and technology are occurring rapidly, and there is an increasing level of convergence among disciplines within the life sciences and in other fields related to agriculture and the agri-food sector. Proper linkages and coordination among government research centres, colleges and universities, and private-sector laboratories will help minimize duplication and foster knowledge and technology transfers.

The Committee heard concerns that the push toward private-public partnerships in agriculture research results in the reduction of independent, government-sponsored agricultural

research that is strictly focused on the public interest. There is a concern that the results of research, or the types of agricultural research undertaken, may be biased if private-sector interests and funds are involved. The Committee supports a strong public funding presence in research, particularly in areas of public concern such as the environment and food health and safety. These are areas where the private sector may have less incentive to undertake research, since they are considered “public goods” and the private sector cannot fully appropriate such benefits.

I criticize the way government, in order to reduce its budget, has gone to private-public partnerships in agricultural research. Of course, all that research will be geared to purely a corporate agenda and not a public interest one. If the results are negative, they do not get published. If the results could be negative, it is not attempted. If it will be in the interests of the public sector as public domain, there is no corporate funding because it is not private. Therefore, we have a severe lack of public interest research in areas like that or in seed development, in livestock genetics, in agricultural practices, et cetera.

Tom Manley, Board Member and Chair of the Ottawa Chapter,
Canadian Organic Growers

Recommendation 14: That the federal government increase funding for agricultural research and development in areas specific to the public interest, such as food safety and the environment.

It is, of course, important to foster an environment that attracts both domestic and foreign private investment funding in research and development. The private sector is more apt to be involved in research that lead to commercialization outcomes and that can generate more immediate returns. This, in turn, can lead to growth in incomes and employment. During Committee proceedings, Pulse Canada mentioned that one of the largest lentil producers in the world invested in Western Canada within the last few years mainly because of Canada’s world-class research system.

A number of witnesses expressed support for the development of a comprehensive national research framework that would include all commodity groups and look at the broad needs of agricultural research. The framework would take into consideration value-added processing and the production systems that feed value-added processing. Economies of scale could be achieved by working cooperatively to undertake comprehensive research in areas such as water management that cut across commodity sectors.

Recommendation 15: That the federal government adopt a comprehensive national research framework that considers broad agricultural research issues across commodity sectors.

One suggestion was to discuss the possibility of introducing a national research check-off program at the producer level that applies across commodity sectors. More broadly, the Committee feels that there is a need for a venue where farmers' views concerning research and development can be discussed across commodity sectors. The Committee would support the expansion of round tables to include one that is focused on agricultural research.

Recommendation 16: That the federal government establish a cross-sector value-added round table focused on issues specific to agricultural research and innovation.

The Committee heard concerns about the decline in, and lack of funding for, government extension services. These services provide information and assistance that help farmers to manage their day-to-day needs. There is a concern that, as governments reduce spending in this area, farmers will lose an unbiased source of information about agricultural inputs and farming practices.

VALUE-ADDED AND TRADE

Given Canada's rich resources, trade in primary resources and bulk commodities has been an historic part of the growth of the Canadian economy. However, generic commodities sold in bulk with lower value-added are sensitive even to small price fluctuations, which means that trade in bulk commodities is vulnerable to low-cost and subsidized entrants on the world market. Canada's well-educated workforce, significant research and technology facilities, food distribution infrastructure, respected safety and quality enforcement and regulatory systems, competent public sector and stable economy put the country in a good position to develop competitive advantages in the agricultural value-added sector which can translate to increased opportunities for job growth and strength and stability in the economy. Moreover, a strong domestic value-added sector can be a source of stability and market security for the domestic primary agricultural sector.

While much of my production is exported as bulk product, the domestic processing markets are often my best option for price and market security.

Ted Menzies, President,
Canadian Agri-Food Trade Alliance

A. International Trade Negotiations

In many countries, the agriculture and agri-food sector is strongly protected and supported by government programs and tariff systems. The sensitivity inherent in this sector explains its relatively late entry into recent international trade negotiations. At the WTO General Council meeting held during 27-31 July 2004 in Geneva, an agreement was reached on a framework for future negotiations. With regard to agriculture, the framework supports reductions in trade-distorting domestic support and improvements in market access for all products. It also commits the parties to eliminating government financing and the underwriting of losses by governments for exporting State Trading Enterprises. The framework sets out the scope for future negotiations and could have long-term consequences for Canada's agricultural sector, particularly for the current operation of the CWB and national supply management agencies.

The Committee heard testimony pointing to major trade impediments to growth in the value-added sector. The use of tariff rate escalation practices by Canada's trading partners was cited as a major concern. Tariff escalation describes the practice of setting lower tariffs on primary bulk products and higher tariffs on processed products. This practice protects the domestic processing of the importing countries and discourages processing in the exporting countries. Tariff escalation has been cited in the WTO framework as an element of negotiation.

The practice of applying higher tariffs on more highly processed products also has a negative impact on Canada's value-added sector. While Korea applies a 40 per cent tariff on beef, it applies a 70 per cent tariff on beef jerky, which is a value-added product. In Japan, the bound tariff on beef is 38.5 per cent but the tariff on seasoned beef such as prepared hamburger patties, is 50 per cent.

Tariff escalation is also a significant problem for the oilseed-processing sector. For example, Japan imports oilseeds free of tariff, but it applies a tariff of about 20 per cent on imports of refined soybean and canola oils. This tariff prohibits access for Canadian oilseed processors, preventing them from competing for a share of the 2.4-million-ton bulk vegetable oil market in Japan.

Ted Menzies, President,
Canadian Agri-Food Trade Alliance

Recommendation 17: That Canada’s WTO negotiations identify, as one of Canada’s priorities, the reduction of tariff rate escalation practices of setting higher tariffs on processed products.

Agriculture and agri-food products are uniquely vulnerable to a wide range and complex set of regulations, standards, testing and certification procedures that are geared to consumer health and safety protection. The high cost of meeting multiple mandatory sanitary and phytosanitary measures in different countries, and the risk that these measures could be used solely as trade barriers to protect domestic industries, have led the WTO to encourage the adoption of international standard codes,⁽⁸⁾ guidelines and recommendations where they exist.⁽⁹⁾ However, members are not bound to respect the standards.

The food processing and distribution industries are subject to a number of regulations that require proper grading, standards of identity, packaging, and labelling. Ted Menzies, President of the Canadian Agri-Food Trade Alliance, observed that the value-added sector is disadvantaged by the lack of understanding or communication between Canadian trade negotiators and Canada’s food processing industry. This can lead to the negotiation of trade implementation agreements and protocols that are ill-suited to the practices of the domestic industry.

Canada negotiated an agreement with China to allow China to accede to the WTO. When we negotiated the framework for that agreement, there was a lot of consultation and good discussion on that basic framework, but when it came to implementing the agreement and it got into detail about, for example, whether the boxes should be a certain size or whether we had to have certain language

(8) The Office international des épizooties (OIE) publishes health standards for international trade of animals and animal products. The Food and Agriculture Organization (FAO) of the United Nations and the World Health Organization (WHO) use the *Codex Alimentarius*, a science-based food standard.

(9) WTO, “Understanding the WTO: The Agreements – Standards and Safety,”
http://www.wto.org/english/thewto_e/whatis_e/tif_e/agrm4_e.htm.

requirements or whether our processors would wear knit cotton gloves, it fell apart, because there was not someone there with an intimate knowledge of what this meant for the industry when they were negotiating those sort of agreements.

Patty Townsend, Executive Director,
Canadian Agri-Food Trade Alliance

It is imperative that the federal government form closer relationships with the food processing sector. Industry experts who have close knowledge of industry practices should be part of the negotiating team during discussions relating to trade implementation agreements. Further, evaluations of negotiation results and procedures should be put in place to improve outcomes in future negotiations.

Recommendation 18: That the federal government consult, and include in negotiations of trade implementation agreements, unbiased industry experts who have extensive knowledge of the processing and manufacturing requirements of the industry or industries that could be affected by these agreements.

1. The BSE Crisis

The BSE crisis caused considerable turmoil in Canada. Nearly all exports of live cattle were immediately suspended after the announcement of the discovery of BSE on 20 May 2003. As observed in the Senate Committee on Agriculture and Forestry interim report, *The BSE Crisis – Lessons for the Future*, Canada relied heavily on the export of live cattle and lacked the domestic meat packing capacity to process its cattle. The BSE crisis highlighted the vulnerability inherent in depending on another nation's infrastructure to process our cattle, particularly since trade in live animals is potentially very susceptible to trade disruptions. It also raised concerns over the concentration in the meat packing sector. In a letter to the chair of the Standing Senate Committee on Agriculture and Forestry, the Minister of Agriculture and Agri-Food Canada made a commitment to explore the Committee's recommendation that part of the venture capital funding announced in the 2004 federal Budget be funnelled into additional value-added capacities in the livestock sector. The Committee is encouraged by the federal government announcement on 10 September 2004 of a strategy to reposition Canada's livestock industry through measures that will include funding to help increase the ruminant slaughter capacity.

Recommendation 19: That the federal government continue to consider innovative ways to use the venture capital funding announced in the 2004 federal Budget to increase value-added capacity in the livestock as well as other agricultural sectors.

B. Interprovincial Trade

The liberalization of internal trade increases a country's standard of living. Provincial regulatory and other barriers, whether or not they are designed to protect and favour provincial industries, increase the cost of doing business, discourage investment and national economies of scale, and may result in multiple inventory lines. They also erode the country's comparative trade advantage. The liberalization of trade, on the other hand, may help smaller value-added farming operations who rely on niche markets, since the marketing of specialized products may require a larger scope to survive. (This can be achieved, for example, through direct selling via the Internet.) The country as a whole benefits if unnecessary barriers to trade are minimized, and if producers and processors have fair access throughout the domestic market.

In 1994, Canada's First Ministers signed the Agreement on Internal Trade (AIT), which came into effect on 1 July 1995. The AIT helped to reduce internal trade barriers, particularly in the case of issues related to labour mobility and government procurement. It also served to raise the profile of internal trade barriers.

The Internal Trade Secretariat is the agency that provides administrative and operational support to committees and working groups under the AIT. The agriculture and food goods sector has been one of the most active sectors in filing interprovincial trade disputes. The Committee is concerned that reviews outlined in Article 902 (expanding the scope and coverage of the Agreement) and Article 903 (review of the framework governing supply managed commodities) of the AIT are apparently not to be completed:

- Article 902.4 The Ministers shall, no later than September 1, 1997, complete a review of the scope and coverage of, and any recommendations for changes to, this Chapter with the objective of achieving the broadest possible coverage and further liberalizing internal trade in agricultural and food goods.
- Article 903.2a The Ministers have, within the framework of their review of Canadian agri-food policy, agreed to undertake a comprehensive review of the framework governing supply managed commodities and implement an action plan towards the development of sustainable orderly marketing systems in the Canadian dairy, poultry and egg industries.

The Committee heard testimony indicating that federal and provincial ministers have decided against pursuing the review called for in Article 902, mainly because the provinces and the industry are focusing on WTO negotiations. The review called for in Article 903 concerning the supply management framework appears to be addressed through federal-provincial agreements used by supply management agencies.⁽¹⁰⁾ Nevertheless, interprovincial agricultural trade issues continue to exist, particularly within the dairy sector. The AIT is a consensual agreement. It provides a venue for averting emerging and potential trade barriers, and its authority derives from a mutual commitment to the terms of the agreement. It is the Committee's view that the tenets of the AIT should be respected. In this regard, the Committee is encouraged by recent assurances⁽¹¹⁾ by the provincial and territorial governments that they will respect commitments made under the AIT, and hopes that the AIT chapter on agriculture and food goods will not be neglected.

Recommendation 20: That the review called for in Article 902.4 of the Agreement on Internal Trade, with regard to the scope and coverage of agricultural internal trade, be tabled as per the Agreement.

Recommendation 21: That the comprehensive review called for in Article 903.2a of the Agreement on Internal Trade, with regard to the framework for governing supply management, be tabled as per the Agreement.

The AIT includes a number of exemptions relating to alcoholic beverages, in the form of non-conforming measures. Canada's *Intoxicating Liquors Act* grants provincial governments sole authority to import alcoholic beverages. The Committee was informed that the provincial monopoly on purchasing alcohol for resale is disadvantageous to small producers, since provinces favour a homogeneous system of stocking core products across their stores and small wineries cannot supply the minimum quantity required to meet the provincial retail model. The Committee is concerned that the present system may favour international wine imports over small domestic wineries.

Recommendation 22: That a review of interprovincial marketing, distribution and access to points of sale of alcoholic beverages be conducted by federal and provincial governments under the auspices of the Agreement on Internal Trade.

(10) It does not include the dairy sector.

(11) In February 2004, the Council of the Federation reconfirmed its commitment to internal trade obligations under the AIT.

CONCLUSION

It is recognized that Canadian governments have programs and policies in place aimed at assisting on-farm and other agricultural value-added businesses strategies. The Committee feels, however, that more aggressive action is needed. As observed during the BSE crisis, an industry becomes vulnerable if it relies too heavily on the processing infrastructure of another country.

The first step is to ensure that regulations and marketing arrangements are designed in such a way that they recognize the need to foster value-added investment, particularly at the farm level. Value-added agriculture widens the opportunities available to farmers by providing options that are not solely restricted to increasing productivity, expanding the size of the farm and competing strictly on the basis of price.

It is not enough, however, for farmers simply to move up the production chain and displace their competitors, or increase competition, within the food processing or other sectors. In broad terms, value-added is rooted in the branding of Canadian products through health, quality, regional or other attributes that respond to consumer demand. It manifests itself in domestic consumer confidence and pride in the foods we produce. This confidence must be fostered also beyond Canada's borders, through knowledge of international customers' needs and trends and through sustained efforts to ensure quality and safety in the production, distribution and marketing of our products.

APPENDIX

WITNESSES

- 30 September 2003** *Agriculture and Agri-Food Canada (AAFC)*
Michael Presley, Director General, Food Value Chain Bureau
Harold A. Hedley, Director, Grains and Oilseeds Division
Susie Miller, Director, Co-operatives Secretariat
Lois James, Director, Renewal Programs
Gilles L. Rousselle, Acting Director General, Research, Planning
and Coordination
- 21 October 2003** *National Farm Products Council*
Cynthia Currie, Chairperson
Ron O'Connor, Vice Chairperson
- Canadian Wheat Board*
Ken Ritter, Chair
Bill Nicholson, Director
Jim Thompson, Senior Marketing Manager
- 23 October 2003** *Internal Trade Secretariat*
Lorraine Andras, Acting Executive Director
- Agriculture and Agri-Food Canada and Canadian Food Inspection Agency (CFIA)*
Ian Thompson, Director, Western Hemisphere, Trade Policy Division
(AAFC)
Steve Verheul, Chief Agriculture Negotiator (AAFC)
Paul Haddow, Executive Director, International Affairs (CFIA)
Debra Bryanton, Executive Director, Food Safety (CFIA)
- 28 October 2003** *Canadian Agri-Food Trade Alliance*
Ted Menzies, President
Patty Townsend, Executive Director
- 4 November 2003** *Canada Beef Export Federation*
Ted Haney, President
- 6 November 2003** *Prairie Pasta Producers*
Perry Mackenzie, Chairman
Allan Brigden, Director

- 1 April 2004** *Pulse Canada*
Gordon Bacon, Chief Executive Officer
Jack Froese, Chair
- 20 April 2004** *Atlantic Beef Producers Co-operative*
Dean Baglolo, Chairman
Bryan Inglis, Member of the Board of Directors
- 22 April 2004** *Canadian Organic Growers*
Janine Gibson, President
Laura Telford, Executive Director
Tom Manley, Chair, Ottawa Chapter
- 27 April 2004** *Quail's Gate Estate Winery*
Tony Stewart, Proprietor
- 29 April 2004** *Agriculture and Agri-Food Canada*
Gary B. Koestler, Deputy Director, Eastern Hemisphere Division,
International Trade Policy Directorate
Michael Presley, Director General, Food Value Chain Bureau,
- Canadian Vintners Association*
Bill Ross, President
- 4 May 2004** *Brock University, Cool Climate Oenology and Viticulture Institute*
Linda Bramble, Industry Liaison
- 11 May 2004** *Ontario Maple Syrup Producers Association*
Mark Wheeler, Member of the Board of Directors
Don Dodds, Chair, Research and Technology Transfer Committee