



Regulatory Barriers Impeding the Competitiveness of Ontario's Food & Beverage Processing Industry

Alliance of Ontario Food Processors

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EXECUTIVE SUMMARY

Introduction

In 2008, the Alliance of Ontario Food Processors, with support from the Ontario Ministry of Agriculture Food and Rural Affairs, completed the *Strategy for Ontario's Food & Beverage Processing Industry* as a plan to guide both industry and government decision and policy making over the next five to ten years. One of the key priorities identified in the Strategy was the need to modernize the regulatory environment to support the future success of the industry. The first step in that process of modernization is to truly understand those regulations that are acting as impediments to the competitiveness of the industry.

The Alliance of Ontario Food Processors, with funding from OMAFRA, contracted with the George Morris Centre to undertake a comprehensive review of the regulatory barriers affecting the Ontario food and beverage processing industry's competitiveness. A number of organizations and individuals were contacted through focus groups, surveys and interviews to identify the specific

regulations that most impede their competitiveness.

The following is an Executive Summary of the findings of the George Morris Centre Report "Regulatory Barriers to Competitiveness in the Ontario Food and Beverage Processing Industry: What are they and What is the Strategy?", along with an Action Plan developed by the Alliance of Ontario Food Processors to address these regulatory barriers. The George Morris Centre Report is appended to this Summary and while all views expressed in the GMC Report may not be shared by all Alliance members, the Report serves to provide a third party assessment of the regulatory challenges facing the Ontario food and beverage processing industry.

Food and Beverage Processing

Matters to Ontario

As the second largest industrial sector of Ontario's economy, food and beverage processing is a major employer (110,000+ direct jobs), a major generator of economic activity in cities and towns across the Province (generates \$33 billion in shipments), a major buyer of the commodities produced on Ontario's farms

(buys 70% of total farm production), and an important stabilizing factor at a time when Ontario's largest industrial sector, auto assembly and auto parts manufacturing, is facing unprecedented structural and market challenges. Ontario consumers may not need to purchase new cars in 2009 but they need to eat every day – and so do the seven billion other inhabitants of our planet. While consumer demand for food and beverages is not completely inelastic, it is much less vulnerable to precipitous swings in consumer spending than many other sectors of the economy -- consumers may be able to defer purchasing a new piece of furniture, a trip to the ball game or a new car, but they will prioritize tomorrow's supper meal.

In order for the food and beverage processing sector to buck the trend towards decline which is affecting the manufacturing sector in Canada's heartland, and realize its potential for growth and to contribute to leading Ontario out of the recession, it urgently needs commitment from both the Canadian and Ontario governments to reform the complex regulatory system in which the sector operates. The goal of the reforms needed is

to improve the competitive position of the sector both domestically and globally while ensuring the safety and quality of the food and beverage products processed in Ontario.

Regulatory Environment

The food and beverage processing industry is a highly regulated industry, affected by legislation enacted and administered at all levels of government: federal, provincial and municipal. Currently Ontario food processors face a difficult competitive environment. Their challenges are compounded by a regulatory system that is burdensome, adds unnecessary costs, hampers innovation and provides disincentives for investment. Further, many processors rely on key inputs in a regulated marketing system that puts significant decision making authority for the entire industry in the hands of farmers. Addressing these regulatory challenges is a critical factor to the future success of Ontario's food and beverage processing industry.

Disinvestment in the industry is a major concern. In a comparison between Canadian and US companies' investment since 2000,

US investment in the food industry grew at a rate of over 20% per year, while Canada's was stagnant to declining. Many studies attribute the lack of investment in the Canadian food and beverage industry and manufacturing in general to Canada's tax structure and its heavy burden of regulation. Ontario ranks among the highest in Canada in both these categories.

The management of companies that process food and beverages in Ontario is constantly assessing whether Ontario is the optimal place for their activities to be carried out. Transnational corporations, which have many options for the allocation of production decisions, can exit from Ontario. Indigenous firms can relocate outside Ontario or decide to downsize or close. Those decisions are not always voluntary. They may be imposed by banks that have lost their appetite for underwriting risks in the food and beverage processing sector. The regulatory environment in which firms operate is a key risk factor that influences decisions about extending credit. Ontario has experienced disinvestment from several major transnational food and beverage processing firms in 2008. The Hershey plant in Smiths Falls, the Pepsico-QTG plant in

Trenton, the CanGro plants in Exeter and St. David's are among recent losses. One way to stem this tide of disinvestment is to signal the importance that Ontario attaches to getting its regulatory environment for the food and beverage processing sector more conducive to doing business here and to implement the reform necessary to achieve it.

The food and beverage processing sector in Ontario is not opposed to effective regulation. There are effective regulations that serve essential roles in protecting the public interest – these regulations have a low-cost-to-high-societal-benefit ratio. But regulation must take into account changes occurring in the way business is done globally and the pace of technological change – many regulations were introduced at an earlier period in Ontario's history before the mobility of capital, goods, services, information and people became a defining characteristic of the way business is done in the twenty-first century. There is no process for a mandatory review to ensure that regulations are keeping up to date with change. Out-of-date regulations are a major barrier to innovation.

Study Findings

A number of common themes emerged throughout the consultation process:

- Governance of Regulated Marketing
- Political Decisions are Made with Limited Consultation
- Inefficient Administration
- Inconsistent Interpretation and Enforcement of Regulation
- Prescriptive Regulations Can Stifle Innovation
- Regulations Create An Unlevel Domestic Playing Field

While a brief description of each of these themes follows more details are provided in the George Morris Centre Report in the Appendix.

Governance of Regulated Marketing

The governance of regulated marketing was cited a number of times as a major barrier. The governance structure (resulting from regulation) in Ontario's regulated marketing system confers significant unilateral decision making authority to producer boards. This approach may have been reasonable in the 1960's when many of

the provincial marketing plans were set up. At that time the scope of issues dealt with by the boards primarily impacted the producers they represented. However, the agri-food industry has evolved over the years to a point where, today, decisions made by the producer boards pursuant to their delegated authority, go well beyond matters affecting just the farmers they represent. The governance structure has not kept pace in providing a broader industry based approach to policy development and decision making.

This issue is not anti-farm, not about dismantling supply management or regulated marketing, and it is not about getting lower prices for commodity inputs. The issue is fundamentally simple: processors want inclusion in the decision making processes on issues that impact the industry and consequently, their businesses. In order to build a healthier industry, respond to changing customer and consumer needs and expectations, and develop true industry partnerships, it is imperative that the system be reformed to keep pace with the environment in which the sector as a whole operates.

In the past, the situation has been compounded by the fact that the government's oversight body, the Farm Products Marketing Commission, has not traditionally been proactive nor engaged in providing oversight for the whole value chain.

Political Decisions are made with Limited Consultation

Representatives of the food industry made it clear that they are often not consulted when policy decisions are being considered that affect the sector. For example:

- Introduction of Family Day, an additional paid holiday
- Changes to the Minimum Wage
- Employment Standards Act
- Stewardship Ontario's Blue Box Program
- Occupational Health & Safety Act's Application to Agri-Food

Inefficient Administration

Inefficient administration of regulation and its enforcement was a common theme throughout the consultations related to regulatory barriers. Inconsistent and imprecise administrative practices have the

effect of confusing and complicating regulatory compliance requirements, increasing costs and delaying regulatory approvals.

Numerous examples were cited that included inadequate communication of regulatory changes, inadequate and/or non-existent training programs to help industry meet the challenges of new regulatory requirements including a lack of guidance materials to provide direction for industry and a lack of avenues to find out when rules have or are about to be changed. The industry also cited a lack of performance measurements that assess the objectives of regulations that the industry must adhere to.

Inefficient administration has direct economic impact on processors. For example:

- Meat inspectors must be present during meat processing activities. However, the current administrative requirements of scheduling inspectors to meet the processing schedule is burdensome and inflexible, resulting in higher costs to processors.

Duplication is also another example of inefficient administration. For example:

- The licensing and auditing requirements for Ontario wineries require nine separate licenses to conduct normal winery practices. In most cases, the same information is required for each license resulting in a large, non-productive and avoidable cost.

While the focus of the GMC Report related to Ontario regulations, federal regulations were also cited that cause barriers to competitiveness such as those that impede the speed at which new food products, crops, new crop protection products and new animal health products can be registered. Furthermore, there is growing concern that Canada's system of regulatory approvals is negatively influencing research, development and innovation in Canada.

Inconsistent Interpretation and Enforcement of Regulation

Inconsistent interpretation and enforcement of regulations was cited in most of the focus groups and interviews. Inconsistent interpretation of regulations is costly to processors and provides them with no

confidence that their actions will result in compliance and can affect consistency of production. Specific examples of inconsistency were cited as follows:

- Meat inspection
- Property Assessment and Taxation – because the *Ontario Assessment Act and Regulations* has not clearly defined agriculture and its value-added activities for property tax assessment purposes, there is inconsistency across the province resulting in unfair advantages for some jurisdictions over others
- Sub-delegation by the federal government of regulatory powers to Commissions or dairy producers in various provinces is not consistent creating competitiveness issues for firms within the provinces

Prescriptive Regulations Can Stifle Innovation

Several regulations are perceived as being in place for political reasons and not necessarily for food safety or quality reasons. The inability to utilize new packaging and labeling, new technologies and new ingredients results in stifled

innovation and are a barrier to compete with non-traditional substitute products. Examples of restrictive regulations which stifle innovation include:

- Lack of adoption of the National Dairy Code which removes the current prescriptive nature of provincial and federal regulations
- VQA packaging regulations only allow glass bottles, while competitors from other countries are using tetra-paks and other unique packaging
- Cheese composition standards – CFIA has no way to enforce leaving processors without the means to achieve efficiencies
- Canada’s fortification policy remains prescriptive while other countries’ have moved forward with food innovation

Regulations Create An Unlevel Domestic Playing Field

The following examples were provided to identify those regulations creating an unlevel domestic playing field.

- Long Combination Vehicles (LCVs) are not permitted in Ontario but are permitted in other provinces

- Different product procurement requirements for wineries that were established pre-1993 and those established after
- Perception of differences in food safety between provincially and federally inspected plants
- Limited number of distribution channels for Ontario wineries and lack of marketing from the LCBO
- Differing compositional standards for some dairy products at the federal and provincial levels
- Escalating interprovincial movement of live chicken between Ontario and Quebec by farmers

Conclusion

Fiscal pressures on government coupled with declining investment levels by business indicate a shared need to tackle the complex maze of regulations that govern Ontario’s food and beverage processing sector. The payback to government will be reduced cost of regulatory compliance through more effective regulations and the payback to industry will be a more competitive jurisdiction in which to do business. In the long run, there is no cost to government to address these regulations

and the payback is a positive impact on business, the public and Ontario's farmers. There is a mutual desire to work together on a new approach to making and reforming regulation for the benefit of Ontario as a whole.

Moving Forward

Addressing the identified regulations and the overriding themes that they fall within will require actions on a number of different fronts. For example, some fall within the mandate of OMAFRA and others fall within the mandate of other provincial Ministries or at the municipal level. Some regulations that have broad impact across the industry will be able to be addressed through the Alliance and others that are more sector-specific, will need to be dealt with by those respective sectors.

The following defines a course of action for both industry and government in tackling the regulatory barriers to competitiveness that have been identified by industry.

Governance of Regulated Marketing

The Governance of Regulated Marketing is the first priority to address as it is distinct from the other regulations. In many sectors

regulated marketing is the foundation upon which the industry operates and for those sectors to be successful into the future, changes must be made to the governance structure now.

Goal: To have equal representation of processors and farmers in decision making bodies where the decisions affect the industry as a whole.

Note: An example of this kind of governance structure, in which responsibility for decision making is shared, currently exists in the regulated marketing system in Ontario with the Ontario Broiler Hatching Egg & Chick Commission. Membership requirements result in consultation and decision making by all parties in the value chain. Membership is made up of four representatives of the Ontario Broiler Chicken Hatching Egg Producers and four representatives of the Ontario Hatcheries Association. Together the eight members appoint a Chair.

Strategy for Addressing Non-Regulated Marketing Regulations and Themes

While many specific regulations have been identified as barriers to competitiveness by the industry, it is the overriding themes that must be addressed if industry is to move

forward and address the specific regulations:

- Political Decisions are Made with Limited Consultation
- Inefficient Administration
- Inconsistent Interpretation and Enforcement of Regulation
- Prescriptive Regulations Can Stifle Innovation
- Regulations Create An Unlevel Domestic Playing Field

Goal: To eliminate the overriding regulatory barriers identified above.

Actions:

In order to address the identified regulatory barriers and meet the ultimate Goals to support a regulatory environment conducive to growth and prosperity of the industry the following Actions are recommended:

- Formation of the Regulatory Modernization Task Force with representatives from government and industry. The Task Force will be responsible for:
 - a) developing an action plan to address the regulatory barriers

and overseeing the changes that are required

- b) initiating a formal review and analysis of the impact of the current marketing board structure (economic, social, etc.), including an analysis of alternative decision-making models in other jurisdictions that are inclusive of all stakeholders
- Develop resources at AOFP to support a regulatory affairs position that will inform industry of regulatory changes, provide input into the development of regulations, and undertake an economic impact assessment of proposed regulations.
 - Develop a one-window access point to assist the industry in navigating the regulatory system.
 - Work with OMAFRA to ensure that industry is aware of regulations across all Ministries as regulations are being developed.
 - OMAFRA to act as an advocate of the food and beverage processing sector with respect to regulations and regulatory development.



GEORGE MORRIS CENTRE

Canada's Independent Agri-Food Think Tank

APPENDIX 1

Regulatory Barriers to Competitiveness in the Ontario Food and Beverage Processing Industry: What are they and What is the Strategy?

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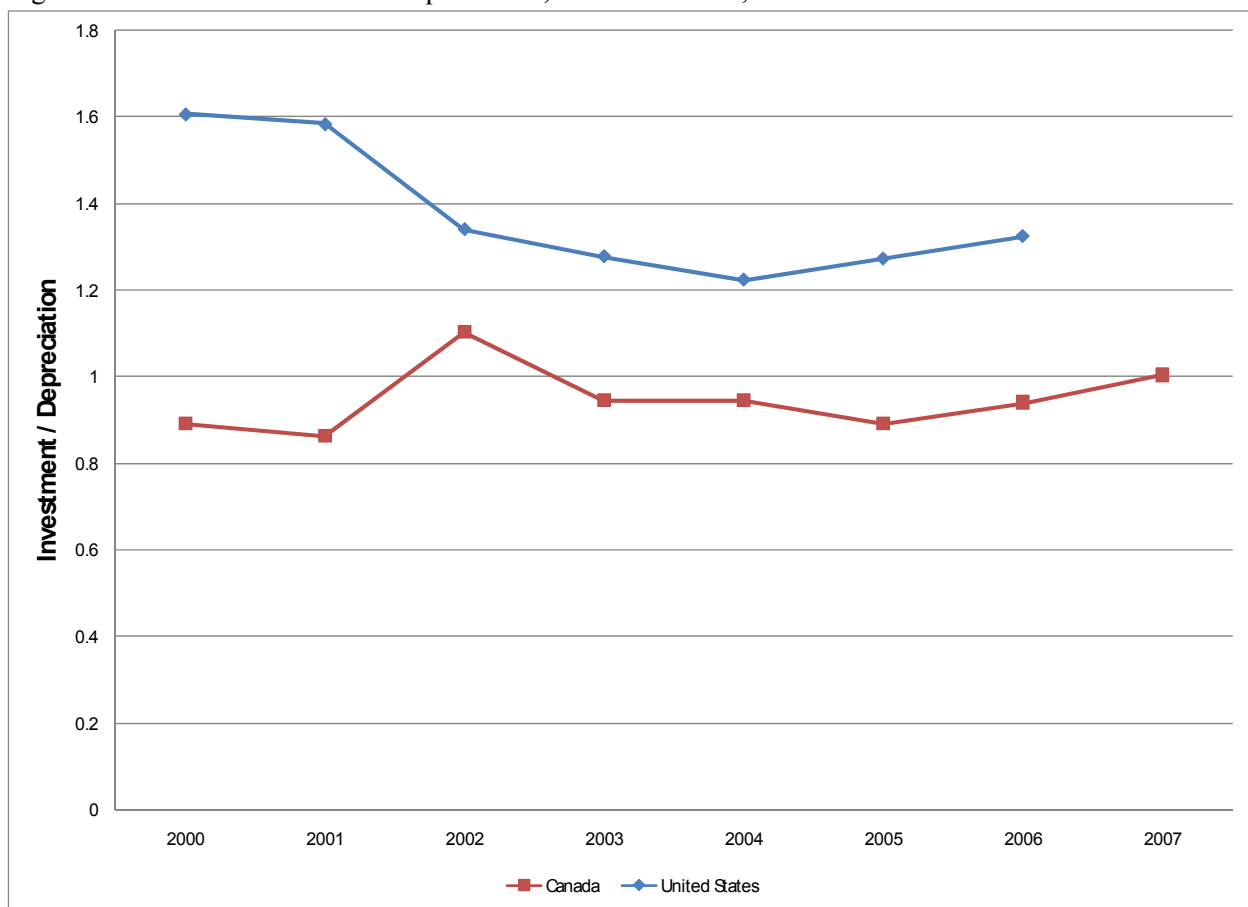
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1.0 Introduction

The food and beverage processing industry is one of the most highly regulated industries, affected by legislation enacted and administered at all levels of government: federal, provincial and municipal. Currently, Ontario food processors face a difficult competitive environment. A rising currency, lagging profitability, and low labour productivity are factors with which food processors must deal. Processors in Ontario perceive that they are handicapped in dealing with some of these issues by a regulatory system that adds unnecessary costs, hampers innovation and provides disincentives for investment.

The lack of investment is both obvious and disconcerting. Figure 1 contains a comparison of investment in the food and beverage industries of Canada and the US for the past 20 years. The comparison shows the ratio of new investment to depreciation. If this ratio exceeds 1.0, it means that new investment is greater than depreciation. Therefore, capital formation is occurring. Conversely, a ratio less than 1.0 means that new investment is not replacing depreciation.

Figure 1: Ratio of Investment to Depreciation, Food Industries, 2000-2007



As can be seen, the ratio for Canada has been less than 1.0 for most of this decade, while the US ratio has been greater than 1.2. This means the US industry's capital base grew at a rate of over 20% per year, while Canada's was stagnant to declining. Growth in capital in the US is the single factor that led to

increasing labour productivity, which exceeds Canada's by 30%. Many studies attribute the lack of investment in the Canadian food and beverage industry and manufacturing in general to Canada's tax structure and its heavy burden of regulation. Ontario ranks among the highest in Canada

Much work has been done to identify and quantify the regulatory burden imposed by federal regulations on the agri-food sector, especially those imposed by Health Canada (Brethour et al. 2004; Brethour et al. 2005; SSAC, 2004; Zecchini, 2006). But very little has been done at the provincial level, despite the fact that food processors have articulated general concerns with the regulatory environment. Interestingly, the government of Ontario does recognize that regulations impose a high cost on industry and is committed to lowering that burden as evidenced by the following statement:

“Ontario’s goal is to lead all Canadian jurisdictions in efforts to measure and reduce the regulatory burden. Ontario’s regulatory modernization will start with an aggressive cap-and-trade initiative for government regulations, so that when new regulations are enacted, others must be eliminated.” March 2008, Ontario Budget 2008. Background: Key Sectors

This is a laudable goal. This report was prepared consistent with the foregoing as a guiding principle. It offers potential solutions that will assist in attaining the goal.

1.1 Purpose

The purpose of this paper is to discuss those components of the regulatory system that Ontario food and beverage processors identify as regulatory impediments to their competitiveness.

1.2 Methods

In order to conduct a comprehensive review the George Morris Centre research team consulted a number of organizations, including AOFP's Group Members through focus groups, surveys and interviews to help identify the regulatory barriers affecting their industry's competitiveness. The participants were asked to provide details for those regulatory barriers, including:

- Is the barrier the regulation itself, or the administration or enforcement of the regulation?
- What aspect of the business does it affect? (Inbound logistics, production, marketing, administration etc...)
- What is the nature of the burden? How does it affect the industry and your operation?
- Has there been any progress made in changing the identified barrier? Has it been identified as an issue by others?
- Are there potential strategies to improve the barrier?

Participating associations and individuals were asked to share materials that had already been written on any of the barriers that were identified in the focus groups and interviews, as to avoid reinventing the wheel when writing this discussion paper.

2.0 Identified Barriers to Competitiveness

The set of specific barriers described by Ontario food processors during the interview and focus group process all fall under a number of common themes which are discussed in this section. As a whole they reflect what is believed to be a lack of political importance assigned to the food industry by the government of Ontario. In general, the industry has often seemed to be treated as an insignificant participant in the value chain.

2.1 Political Decisions are made with Limited Consultation

It was made clear that the food industry is not regularly invited to have meaningful input into major political decisions that affect it and feels that in most cases regulatory changes are made without consultation of the entire value chain. Examples of this include:

- Recent introduction of Family Day
- *Employment Standards Act*
- Stewardship Ontario's Blue Box Program
- Occupational Health and Safety Act's application to agri-food

For example, in a sector that works with both seasonal and perishable products special circumstances exist in everyday operations. However, there is no process or inclination on behalf of regulators to take into account the special circumstances of the sector and seek input into how to affectively deal with them. The *Employment Standards Act and Regulations* is again a case in point. Due to the seasonality of the industry and the perishability of food products, companies in the vegetable or fruit packing industries and the labour they hire understand the timely nature of their peak packing periods and the time commitment required. Very few other industries are in the same position. But consideration of its special circumstance has never materialized in the Employment Standards Regulations.

This regulatory issue is not new. The Minister's Strategic Advisory Committee (2007) was informed of the lack of consultation during the development of regulations. They have therefore recommended that the government seek all stakeholder input during the development of regulations. To date, it would appear that little has changed.

2.2 Inefficient Administration

Inefficient administration of regulation and its enforcement was a common theme throughout the discussions of regulatory barriers. Unclear administration has the effect of confusing and complicating regulatory compliance requirements, increasing costs and delaying regulatory approvals.

Numerous anecdotal examples were cited that included inadequate communication of regulatory changes, inadequate and/or non-existent training programs to help industry meet the challenges of new regulatory requirements including a lack of guidance materials to provide direction for industry and a lack of avenues to find out when rules do change. The industry also cited a lack of performance measurements that assess the objectives of regulations that the industry must adhere to.

It is understood that certain regulations are necessary. However, without adequate training to fully understand compliance requirements and enforcement, both can be inefficient and an uncertainty exists regarding the cost of compliance. It was also cited that often, when rules change processors are not made aware of the changes until they are found out of compliance with the regulations and then are subsequently penalized or charged.

The inefficient administration of programs that are required for day to day operations result in economic impacts to processors. For example, meat inspectors must be present during meat processing activities. However, the current administrative requirements of scheduling inspectors to meet the needs of a processing schedule have been cited as burdensome and inflexible, resulting in higher costs to processors.

Regulations that impede the speed at which new food products, crops, new crop protection products, and new animal health products can be registered reduce the capacity for competitiveness of the agri-food industry (Brethour et al. 2004). There is growing recognition that Canada's system of regulatory approvals is negatively influencing research, development, and innovation in Canada. Both research results and industry experience indicate significant problems in the federal regulatory approval systems in animal health products, seed registration and in crop protection products (Brethour et al. 2004; Brethour et al. 2005; Seed Sector Advisory Committee, 2005; Zecchini, 2006). In these areas, Canada lags behind other regions in the clarity of the approval process, consistency in data and experimental result requirements, and in the time required to make approval decisions.

As the level and complexity of regulation grows, so does the paper burden of those who must comply. Some aspects of regulation overlap municipal, provincial and federal jurisdictions. The Minister's Strategic Advisory Committee (2007) acknowledged that the approval process for new input products has created a backlog of pending approvals. MSAC cites that part of the problem is the duplication of approval requirements. MSAC recommended that the Minister of Agriculture, Food and Rural Affairs "champion modifying the current regulatory system with counterparts in other governments to ensure that it is more efficient timely" with respect to the approval of pesticides and veterinary drugs (MSAC, 2007).

This issue of duplication also exists with respect to licensing and auditing requirements of Ontario wineries. Wineries require as many as nine separate licenses to conduct 'normal' winery practices in Ontario. In most cases, the same information is required for each license submission. Streamlining these requirements would help to reduce the large, non-productive and avoidable costs that these mainly small Ontario businesses currently experience. This overlap is not confined to licensing. It is similar for the audits conducted by the LCBO and federal authorities.

2.3 *Inconsistent Interpretation and Enforcement of Regulation*

Inconsistent interpretation and enforcement of regulations was cited in most of the focus groups and interviews conducted. This is consistent with the findings of the Minister's Strategic Advisory Committee (2007). Inconsistent interpretation of regulations is costly to processors and provides them with no confidence that their actions will result in compliance and can affect consistency of production. As well, a

program that does not have an adequate and consistent enforcement mechanism can result in a cost disadvantage to those who comply.

A number of examples were cited:

- Meat inspection is notorious for inconsistency in enforcement. This lack of consistency may stem from a lack of adequate training and therefore decisions are left to the interpretation of individual inspectors. This has resulted in the new interpretation of old regulations. Effective guidance and accountability for inspectors has long been recommended.
- Property Assessment and Taxation: The Ontario Ministry of Agriculture, Food and Rural Affairs has encouraged value-added, differentiation and collaborative activities on-farm and between farmers and processors as a way to add profitability to operations. However, these activities have caused confusion in the interpretation of what constitutes farming in the province's property tax assessments and as a result is affecting classifications and tax rates.

The fundamental problem is that the Municipal Property Assessment Corporation¹ (MPAC), which implements the Ontario Ministry of Finance's *Ontario Assessment Act and Regulations*, has not clearly defined agriculture and its value-added activities for property assessment purposes. This has resulted in inconsistent classifications around the province. This inconsistency can have an effect on decisions to innovate on small operations because the difference in tax between agriculture and industrial is greater than the early profits.

- The federal government has sub-delegated regulatory powers to Commissions or dairy producers in various provinces. There is inconsistency among provinces, which creates problems for industries within the provinces. This has been long recognized as evidenced by the allegation that inconsistent administration "renders regulatory interpretation and change more unpredictable and less transparent than if powers remained at federal level" (Smith et al. 2005)

If regulations are to be implemented, then the government must have the resources to effectively and efficiently enforce them on a consistent basis. The Minister's Strategic Advisory Committee (2007) recommended to the Minister that the government must improve consistency in applying and enforcing regulations through the harmonization of regulations, standard inspection training programs and developing performance measures.

2.4 Prescriptive Regulations Can Stifle Innovation

Some regulations are so prescriptive that they clearly stifle innovation.

- One issue is the National Dairy Code which was compiled 10 years ago and has yet to be adopted. It is a compendium of all regulations and it is not prescriptive. Instead the regulatory system retains specific rules regarding size of packages, material of packages, (EPA Reg. 344 & 345) and package types that can be used. For example, glass bottles are not actually approved but tetra-paks are.

¹ MPAC is the provincial organization charged with assessing property uses and establishing the taxation class for all land and buildings in Ontario.

- Ironically, a complaint from some in the wine industry is that VQA packaging regulations only allow glass bottles, while competitors from other countries are using tetra-paks and other unique packaging.
- Other examples include cheese composition standards, which the industry states CFIA has no way to enforce, and processors have no way to comply.
- Canada's food fortification policy remains very prescriptive with respect to the types and levels of vitamins and minerals that can be added to foods. Whereas, other countries' fortification policies have moved forward with food innovation while Canada is missing out on significant market opportunities.

Some of these regulations were put in place for political reasons, and not necessarily or exclusively for food safety or quality reasons. The inability to utilize new packaging and labeling, new technologies and additives results in stifled innovation and are a barrier to compete with non-traditional substitute products. A number of these standards are likely difficult if not next to impossible to enforce, thereby creating an unlevel playing field between those who are in compliance and those who may not be.

2.5 Governance of Regulated Marketing

Regulations that influence the procurement of farm products by processors and handlers are pervasive in Ontario. Regulation influences the following aspects of farm product marketing/procurement:

- prices paid for farm products
- means of determining prices paid for farm product,
- quantity of product produced/available for purchase
- settlement terms with producers
- product delivery terms and standards
- product standards and quality
- dispute resolution and remedies

The regulatory oversight authority for marketing regulations is vested with the Ontario Farm Products Marketing Commission (FPMC), which, in turn, delegates the implementation of regulatory authority across commodities to producer marketing boards. In practice, marketing boards administer marketing regulations in Ontario, and report periodically to the FPMC.

In the focus groups, participants raised a number of issues regarding regulated marketing based on their own experience. These are summarized below:

- Regulation imposes adversarial relationships with producers and limits scope of cooperation and information sharing
- Regulation has had the effect of vesting decision making rights with producers so they can (and do) act unilaterally.
- Arbitration is not an optimal way to establish price.
 - Arbitration processes are awkward, inefficient, adversarial and costly.
 - The process does not ensure the outcome of a fair or correct price. Instead, it often comes down to arguments among lawyers, which may or may not have anything to do with the value of a product. Moreover, the process is very expensive.
 - Allows parties to drop out of negotiation and opt for arbitration.
 - Arbitration doesn't necessarily bind producers because they can opt out of growing for a processor and not sign a contract, while processors are obligated by the arbitration decision (supply management is an exception to this).

- Decisions from arbitration create precedents that are used in later negotiations, so the impact of a single arbitration can have long standing effects. While some precedents are clearly positive, others are not. Yet, because of the system, the process often must incorporate poor arbitration decisions going forward.
- Regulated marketing, in some cases, has difficulty dealing with differentiated products, and tends to impose uniformity of product attributes. For example, price mechanisms that seek to pay producers according to specific attributes that are important in differentiation today but were not important historically are difficult to get implemented.

There are two primary issues based on the notes above:

Governance

All decision making for regulations rests in one part of the supply chain. Decisions are made by primary producers, with no requirement for (and in many cases no) consultation with those downstream. The result of this is that the system is built on a foundation of adversarial relationships and makes it virtually impossible to establish value chains, or to improve value chain efficiency.

FPMC is not proactive, is disengaged and does not provide oversight for the whole value chain. The system simply remains adversarial, does nothing to encourage good supply chain management, and discourages innovation. Farm Products Marketing Commission is supposed to be a third party, but that it

Ontario Broiler Hatching Egg & Chick Commission

Membership requirements result in consultation and decision making by all parties in value chain.

- Ontario Broiler Chicken Hatching Egg Producers appoint four members
- Ontario Hatcheries Association appoint four members
- Together the eight members appoint a Chair.

almost always favours farm producers. This is a structural problem that arises because of the legislation. The legislation establishes *producer* marketing boards, not *industry* marketing boards. In its legitimate and well meaning attempt to protect farmers from being exploited by those with market power, the legislation shifted the focus of market power.

The uncertainty created by this regulatory environment results in reduced investment in Ontario. One person we interviewed gave two specific examples. In both cases, his company's investment analysis slightly favoured Ontario, but the final decision was made in favour of another jurisdiction because of regulated marketing in Ontario. One trend the food sector faces is toward consolidation by multi-nationals. In this circumstance, investment decisions are made based on payoff and risk, not on national or regional considerations. This illustrates the dilemma created by a system that places all decision making power in one component of the supply chain; decisions are not made to improve the efficiency of the chain, triggering additional decisions downstream that further weaken the efficiency of the supply chain and reduces innovation, thereby reducing competitiveness.

It is interesting to note that Canada's competitors have either avoided or abandoned marketing systems that concentrate power in one component of the supply chain. With respect to innovation and research Holland, Denmark, Australia and New Zealand have all opted for systems with direction from "commissions" that represent the entire chain and that share decision making power among market

participants. The industries in Ontario also point to the Ontario Broiler Hatching Egg & Chick Commission membership requirements as an example that works far better for the overall health of the industry.

Overall, regulated marketing has been established to place all the decision making power in one part of the supply chain. Processors are left out with a resulting loss of competitive advantage and limited investment in plant and equipment.

If Ontario is to prosper, then Ontario needs to move to a supply chain type of administrative structure. Processors need to be part of the regulatory decision making process. The Farm Products Marketing Commission needs to oversee processes that will ensure a regulatory system that protects market participants from the abuse of market power, but simultaneously enhances Ontario's competitiveness.

One Price Fits All No Longer Fits

This is a particular issue for the wine industry, where one price is negotiated for each varietal of grape. The only quality marker is brix of sugar content. The result is a system that is misaligned with the marketplace. It results not in a minimum price, but rather a targeted average price with which higher valued grapes subsidize lower valued grapes. Wineries cannot reward quality or purchase grapes based on their end-use. Instead the system promotes yield at the expense of quality. This becomes an increasing problem as international competition increases. The situation results in two outcomes, neither of which is in the best interest of independent vineyards in Ontario. First, wineries increasingly grow more grapes themselves so they can control quality. Second, those wineries that can purchase more juice from offshore sources because they can equate quality with price and can compete at lower price points.

The wine industry advocates for a system in which pay is based on quality and attributes as occurs in other jurisdictions. Ironically, it already exists for processed vegetables in Ontario. The Wine Council of Ontario has been trying to get this changed for several years but, again, every FPMC-led effort has failed. This is another example of the challenges faced when attempting to modernize the system.

2.6 Regulations Create Unlevel Domestic Playing Field

A number of identified regulatory barriers within Ontario have the effect of creating an unlevel playing field domestically, either within Ontario or Canada.

Examples include:

- Long Combination Vehicles (LCVs) are defined broadly as any combination vehicle that is longer than normally permitted, for example double 53-foot trailers. These types of vehicles are not permitted for use on Ontario highways, but operate by special permit in most other provinces and have been allowed for use in Quebec for 25 years.
- It was acknowledged that there is an unlevel playing field regarding product procurement practices between wineries that were established pre-1993 and those established later. No other jurisdiction in the world has separate product procurement policies based on establishment differences.

- Ontario has positioned its provincial meat inspection program as a world class system. For example, OMAFRA's HACCP Advantage Food Safety Programs are based on internationally recognized CODEX Alimentarius requirements and harmonize HACCP standards with those of federally-registered plants. The reporting and record keeping requirements under the *Ontario Meat Regulation* mirror that of the *Meat Inspection Act*. However there is a perception of differences in food safety between provincially versus federally inspected plants. In reality, if the government truly thought that the Ontario system was less safe then it wouldn't exist. The federal government won't provide an unequivocal statement regarding the two systems' similarities and recognize their equivalency. A move toward national meat standards would align the provincial and federal safety systems. However, this initiative has gone nowhere. Food safety is different than building requirements for trade, trade requirements should never have become a part of meat inspections.
- Ontario's wine laws and regulations stifle wineries' market access to domestic consumers, compared to other provincial regulating bodies. With respect to market access, there are two fundamental issues, the limited number of distribution channels for Ontario wineries and the lack of marketing from the LCBO. Limited growth opportunities result from limited domestic market access. As a result it is difficult for Ontario wines to get introduced to the market and all wine operations are affected if they can't grow the market. Limited foreseeable growth affects every aspect of the operation from production up.
- Wineries established after 1993 are not allowed to produce blended wines using any foreign content. In the Wine Content and Labeling Act, 2000 s.5 (1) b. it states that the Lieutenant Governor in Council can make "regulations that prescribe conditions under which wineries may use imported grapes or grape products in the manufacture of wine". This rule is not found in the regulation but is included in policy administered by the Alcohol and Gaming Commission of Ontario (Clayton, 2008). "Wineries established before this time can make their own business decisions about whether or not blended wines would be a good addition to their customer offerings" (WCO, 2006). This creates an unlevel playing field regarding product procurement practices among wineries whereas no other jurisdiction in the world has separate product procurement policies based on date of establishment.
- There are differing and overlapping dairy product standards among provincial and federal jurisdictions. At the federal level both the Food and Drugs Regulations (Division 8: Dairy Regulations) and the Canadian Agricultural Products Act (Dairy Product Regulations) contain compositional standards for fluid and non-fluid dairy products. Smith et al. (2005) also provide examples of provincial regulations of compositional standards that do not align with federal standards. For example, differing yogurt standards exist in Manitoba, Quebec, New Brunswick and Nova Scotia (Smith et al. 2005). Quebec has standards for calorie-reduced butter, Manitoba has standards for eggnog and New Brunswick has standards for a variety of cheeses (Smith et al. 2005). In their analysis Smith et al. (2005) recommend that a clear set of compositional standards at the federal regulatory level is required in order to facilitate easier interprovincial trade. It is also clear that the Agreement on Interprovincial Trade (AIT), whose purpose is to facilitate interprovincial trade, has not had any 'teeth' thus far.
- The issue of interprovincial movement of product was brought up by the processors of supply managed products. There are two aspects to this issue. First, that there is essentially a lack of complete regulatory items in that producers have the ability to move live chicken interprovincially which is essentially a loophole in the supply management system. The rules of supply management work within the confines of the province, but do not take into account interprovincial movement of product. This loophole counteracts the security and stability of supply to processors. Interprovincial trade needs to be addressed within the regulatory environment, especially collectively between Ontario and Quebec in order to address the loophole.

2.7 Summary and Conclusions

The Ontario food and beverage processing industry is an important piece of the value chain, it is the:

- #1 purchaser of Ontario farm products
- 2nd largest manufacturing sector in Ontario
- 3rd largest food cluster in North America

(AOFPP, 2008)

As a result, the industry has wide-ranging economic and social importance.

However, if the food industry was truly regarded as a politically important part of the value chain, a number of these regulatory issues would not arise. While there are recent signs of change, there is a long held perception that the food industry in Ontario has no true representation and has problems advancing issues. The industry has the same problem at the federal level.

Ontario needs a structure in place in which the food industry has a champion at the cabinet table in order to have the opportunity to make changes that will result in new opportunities for expansion and growth. An example of this would be the automotive industry which has made clear progress with the government and has regular meetings with the Minister.

The identified regulatory barriers are not new and therefore should not be surprising. In fact, some of these issues have existed for years. Many of the provincial administrative challenges experienced by the industry are the same challenges faced at the federal level. In order to meet consumers' changing and varied demands, processors require a regulatory environment that allows them the ability to innovate and produce products for the future.

3.0 A Strategy to Improve Ontario’s Regulatory Environment for the Food Industry

To develop the strategy, the steering team for the project identified the optimum outcome for each of the issues identified in section 2.0. Second, the team identified the optimum approach to achieve the optimum outcome for each. Third, the various approaches were brought together into an overall strategy.

The result of the process is a strategy with three common components. The first addresses making and implementing regulatory policy. The fundamental concerns about these areas are common as are the approaches to dealing with them in the strategy. These areas are:

- Political decisions are made with limited consultation
- Inefficient administration of regulations
- Inconsistent interpretation and enforcement of regulations
- Regulations create unlevel playing fields.

The second component is the area entitled “prescriptive regulations can stifle innovation”. It has elements common with the group above, but is kept separate because it arises from a point of principle – ie are regulations with no safety objective and no scientific basis appropriate in a market economy?

The third area is regulated marketing. The two issues identified here – governance of the Farm Products Marketing Commission and governance of marketing boards are clearly related.

As implied above, the approach taken was to address specific issues and then build common elements from the specifics. In doing so, it became apparent that a set of principles is needed upon which to develop and evaluate regulatory policy. If one existed, it is strongly perceived that the Ontario food and beverage processing industry would not be facing the regulatory issues it currently faces. Therefore, it is recommended that regulatory policy in Ontario be developed, monitored and evaluated using the guiding principles presented in section 3.1. A second recommendation is that policies be changed following the implementation guidelines discussed in section 3.2 – 3.4. The latter contain recommendations for both the government’s role and AOFP’s role in shaping those changes.

3.1 Principles of Regulatory Policy

Principles are fundamental to the development, implementation, performance and its monitoring of a regulatory system. For example, a government agency or program should have clear objectives in order for it to be monitored and evaluated. If society agrees to a set of principles, then it has them against which to judge the performance of the regulatory system.

Accordingly, as part of a strategy to improve regulatory policy for the agri-products sector in Ontario, the following principles of regulation are presented.

1. Policy should be made with a mindset toward enhancing the competitiveness of industries, not parts of industries.
2. Regulatory policies should have clear and measurable objectives.
3. Technical regulations should:

- a. Be intended to protect human, animal, plant or environmental health.
 - b. Be based on the best available science.
 - c. Be enforceable.
 - d. Be preceded by an analysis of their expected effectiveness and their expected economic impacts and the analysis should be made available to all.
 - e. Not be put in place without appropriate gazetting and adequate time for industry to respond, with knowledge of the impact analysis.
 - f. Be accompanied by processes to measure their actual economic impacts.
 - g. Be financed and staffed to enforce the regulations effectively, including adequate staff training.
 - h. Not be designed to give competitive advantage.
4. Marketing regulation:
- a. Should be made to advance the industry, not just certain aspects of it.
 - b. Should be made with representation from the entire industry, not just certain aspects of it.
 - c. Should be made by open and transparent processes.
 - d. Should be led by independent Chairs with no vested interest.

3.2 Making and Implementing Regulatory Policy

In this area the optimum strategic outcomes are:

- The food and beverage processing industry meets regularly with relevant ministers, deputy ministers, is consulted on policy and program issues and its input is listened to and acted on.
- Regulations affecting the sector are administered efficiently, transparently and with enough resources to be able to do so.
- The industry is confident that all regulations are interpreted and enforced in a consistent manner across the province.
- The industry is confident that regulations are interpreted and enforced consistently.
- Each set of regulations that create unlevel playing fields need to be reviewed and revised.

Actions required to achieve the optimum outcomes are:

- Industry needs to be its own champion. This is envisioned and should be done by strengthening the AOFP.
 - The industry has not been well represented at the political level. While some improvement has been made in the past few years, the analysis in this report shows that much is still to be accomplished.
 - The industry is in part to blame because it has not represented itself well. Hence the need to implement the proposed structure of AOFP and obtain improved resources for its functions.
 - Therefore a key role is to gain profile so that the food and beverage sector is forefront in the minds of politicians
 - To do this, AOFP needs to build the Industry's image to industry decision makers.
 - AOFP needs to impress the importance and size of the industry upon the political system to ensure that government comprehends the impact of its decisions.
 - AOFP needs to secure opportunities for regular twice-yearly briefings on industry issues with Ministers and Deputy Ministers of importance to the food and beverage processing industry.

- The Minister of Agriculture Food and Rural Affairs must represent and be seen to represent the needs of the entire food and agriculture sector in government/cabinet, not just primary agriculture.
- The technical regulatory system needs to be changed substantially and so does AOFP's role in it:
 - AOFP needs to develop a staff position(s) in regulatory affairs that help find and organize regulatory notices in the short term and, in the longer term, drive the following reforms of regulatory processes:
 - Industry needs to be made aware of regulatory changes being made in order to act upon them and be consulted. This should be done by the provincial government putting in place a gazetting process similar to that administered by Health Canada that gives industry notice and response time to upcoming changes in all regulations.
 - Assurance, before a regulation is gazetted, that an economic impact assessment is done, and shared with the industry. Sufficient resources must be available to capably enforce and do ongoing economic impact assessment.
 - Government needs to develop a 'one-window' access point to assist members of the agri-products sector in navigating different regulatory approval and policy processes – as proposed in the AOFP Food and Beverage strategy.
 - Before a regulation is implemented, there is sufficient training of staff to implement and enforce it.
 - Measureable performance standards and assessment processes need to be developed regarding the effectiveness of the regulation, the efficiency of its implementation and its actual impact on the industry.
- The Government of Ontario needs to reduce regulatory duplication and overlap both within its own jurisdiction and where it has joint jurisdiction with the federal or local governments. AOFP must address the specifics here as part of its regulatory affairs mandate. The areas of interest are:
 - Winery Licences.
 - Consistent Training across the province, this must be continuously updated.
 - This will help to eliminate jurisdictional differences in health units, the municipal blue box program, property tax assessment.
 - Policy and procedure manuals and interpretation bulletins should be developed and training provided.
 - Communication of changes in standards/procedures to industry as well as employees.

3.3 Reforming Regulations that Create Unlevel Playing Fields

The desired strategic outcome is to review and reform the specific areas identified under this issue.

As part of its mandate, the AOFP and the provincial government need to work together to develop a process for regulatory review of the areas identified in this category. The review process will be based on the principles identified above to determine first whether there is a justification for them and, if so, whether the regulations and their application are consistent with the principles. If not, then the regulations should be reformed to bring them in line.

3.4 Governance of Regulated Marketing

Outcome: A business environment that is optimal for the value chain.

There are two sets of action items: to improve the governance of the FPMC and to improve the governance of marketing boards.

Actions:

Governance of FPMC

- The FPMC must be engaged and proactive in the process. It needs to be accountable to its mandate.
- The FPMC must provide a balanced approach to industry decisions. Although it is in their terms of reference to ‘take into account the good of the public’, experience suggests this has not generally been the case.
- Commission members should have experience and vision. Performance evaluation of members should be done annually.
- Membership of the Commission should represent the value chain in a balanced way.
- There should be an independent appointment process outside the political system. Legally, appointments must be confirmed by cabinet, but an independent nominating process can be established that recommends members to cabinet.
- There should be clear qualifications for the Chair, including that this person should be from outside agriculture and agri-food, and have strong business acumen.
- Decisions of the Commission should not be appealable to The Agriculture Food and Rural Affairs Appeal Tribunal.

Governance of Regulated Marketing

- There should be equal representation of processors and farmers in decision making about factors affecting the industry.

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