Early Payment Option contract details

EPO components

There are two components that comprise an EPO contract:

1. Early Payment Value (EPV)
2. Discount (time value of money, risk and administration)

EPV

The EPV is equivalent to 80, 90 or 100 per cent of the PRO for the corresponding reference grade and is quoted in Canadian dollars per tonne in store Vancouver or St. Lawrence. The EPV is based on the PRO value in effect on the day the EPO contract is signed.

80 per cent EPV = reference grade PRO x 0.80

90 per cent EPV = reference grade PRO x 0.90

100 per cent EPV = reference grade PRO x 1.00

Discount

A discount for risk, time value of money and program administration is deducted from the EPV that is locked in at sign-up. There are separate discounts for each EPV level. Discounts are posted on the daily pricing schedule. The discount is deducted from the EPO additional payment issued by the CWB following delivery.

1. Time value of money – represents the cost in lost interest of financing earlier payments to producers. However, producers recover this discount on a pro-rated basis according to the actual month of delivery in the form of an incremental payment, which is established at sign-up. (See incremental payment, page 15.)
2. Risk – this discount is taken to offset the risk the CWB is assuming and the cost of hedging this risk using various North American commodity futures and options markets.
3. Administration – covers the cost of administering the program.

Contractual obligations

Terms and conditions

The EPO is a legal contract and producers who commit grain are bound by the terms and conditions of the contract. Definitions, sign-up methods, obligations, pricing information and provisions of the contract are described in the terms and conditions. Before making a commitment, producers should be familiar with these obligations. Terms and conditions are available on the CWB Web site under "Farmers-Producer Payment Options" and through Fax on demand. They can also be obtained by calling the CWB.

Delivery requirement

A key requirement of the EPO terms and conditions is that producers deliver 100 per cent of the tonnage committed to the contract. Also, it is important to remember that the EPO does not have associated delivery terms. Producers are obligated to sign a CWB delivery contract and wait for contract calls so that they can designate deliveries to their EPO.

Changing contract commitments

The EPO program offers several options for reducing contract commitments if producers are unable to meet them. Producers may assign or buy out all or part of their contract. In cases of misgrades, there is a quality transfer clause that allows switching between milling and feed quality wheat and durum and selected and feed barley contracts. If a producer chooses not to exercise any of these options and there is shortfall tonnage on the contract, pricing damages will be assessed.

Assignments

If a producer wants to reduce their EPO obligation, they may transfer all or part of their tonnage commitment to one or more producers. The producer must complete an assignment form, available only by contacting the CWB, specifying the contract number and tonnage to be transferred. The CWB will provide the details of the contract and terms and conditions along with the assignment form. It is the assignor's (producer transferring the contract) responsibility to ensure the assignee (producer taking over the contract) receives the contract information. The form must be signed by both producers and returned to the CWB by fax or mail. A $15 administration fee per transaction is charged for assignments.

Buyouts

Producers can initiate a buyout at any time after making the initial commitment. The buyout cost on an EPO is established at sign-up. Market conditions do not impact the buyout cost on an EPO.

Buyout cost = Discount – time value of money, plus a $15 per transaction administration fee

Producers must call the CWB with their ID and PIN numbers to receive a buyout quote or to execute a buyout transaction.

Quality transfers

If producers are unable to fulfill their EPO contract commitment due to grading changes, they may want to consider a quality transfer, rather than an assignment or buyout. However, buyouts should be considered in conjunction with the quality transfer to determine the lowest cost alternative.

Producers can switch between milling or malting quality EPOs and feed EPOs for a transfer fee. The transfer fee is based on the EPO discount of both classes and measures the arbitrage cost of switching between feed and non-feed classes. Also, a risk premium (referred to as the "roll fee") is charged to cover the CWB's additional risk associated with transferring the contract. The roll fee is $1 per tonne for 100 per cent EPVs, $0.50 per tonne for 90 per cent EPVs and $0.25 per tonne for 80 per cent EPVs. A $15 per transaction administration fee will also be assessed.

EPO transfer fee = (original discount of existing EPO – current discount of existing EPO) + (current discount of transfer EPO – original discount of transfer EPO) If negative, then zero. Plus applicable roll fee and $15 per transaction administration fee.

Once the transfer is completed, the original EPO contract will be cancelled. The producer will receive an EPO contract for the transfer class based on the values on the original contract date. The transfer fee, risk premium and administration fee will be deducted from the producer's next CWB payment.

Example:

A producer signed up a selected barley EPO on August 15 with an EPV of 90 per cent. On October 1, the producer contacted the CWB to advise the barley had been downgraded and request a transfer to a feed barley EPO.

Date	Class	EPV ($ per tonne)	Discount ($ per tonne)
August 15	90 per cent two-row	$225	$7
	90 per cent feed	$135	$4
October 1	90 per cent two-row	$225	$5
	90 per cent feed	$135	$5

EPO transfer fee = (original discount of existing EPO – current discount of existing EPO) + (current discount of transfer EPO – original discount of transfer EPO) If negative, then zero.

Plus $0.50 per tonne roll fee
= ($7-$5) + ($5-$4) + $0.50
= $3.50 per tonne plus a $15 administration fee

The selected barley EPO would be cancelled and the producer would receive a 90 per cent feed barley EPV of $135 per tonne with a discount of $4 per tonne.

Producers may transfer less than the full contract amount, however transfers must be of the same tonnage and EPV level. For example, if a producer wants to transfer a 50 tonne feed barley EPO with a 90 per cent EPV, the selected barley EPO also must be 50 tonnes with a 90 per cent EPV. If the producer has more than 50 tonnes of barley selected and wants an EPO for the entire amount, a second EPO contract can be signed up at current market values to cover the additional tonnes.

If the EPV level of either the original contract or the transfer class has been terminated, a quality transfer cannot be executed. The original contract must be bought out.

Quality transfers can be completed by calling the CWB and providing the producer's ID number and PIN.

Feed and selected barley EPO transfers

If the transfer occurs after January 31, during feed barley Pool B, the producer is still eligible to receive a feed barley EPV and discount that were established during Pool A, but will receive the initial payment for feed barley Pool B. The producer is eligible for future CWB payments if the final pool value of Pool B exceeds the EPV.

The quality transfer only applies to the EPO commitment not the delivery commitment. Producers can complete a Rejected Selected Barley Form to transfer the delivery commitment. In the case of a feed barley Guaranteed Delivery Contract (GDC), the misgrade must be completed prior to expiration of the 30 day delivery period.

Pricing damages

Pricing damages are charged if a producer fails to apply all deliveries to an EPO by the end of the crop year. Pricing damages are equal to the buyout cost, which is established at the time of sign-up.

Pricing damages are charged to ensure the CWB recovers the hedging costs associated with the discount. The EPO pricing damages are fixed and will not change in value following contract commitment.