CWB to sell itself, in secret and not necessarily to the highest bidder

National Farmers Union analysis of recent developments regarding CWB privatization, October 2014

The National Farmers Union (NFU) is a direct-membership voluntary organization made up of Canadian farm families who share common goals. It is the only farm organization incorporated through an Act of Parliament. NFU members believe that the problems facing farmers are common problems, and that farmers producing diverse products must work together to advance effective solutions. The NFU works toward the development of economic and social policies that will maintain the family farm as the primary food-producing unit in Canada.

In late 2011, the federal Conservative government rushed legislation through Parliament to destroy the single desk authority of the Canadian Wheat Board (CWB).[1] The single desk authority was legislative power that ensured all prairie wheat and barley sold for export or for human consumption domestically, was marketed in the interests of farmers, and that all proceeds of grain sales, net of operating costs, were returned to farmers each year, as retained earnings were not permitted. The CWB was not a grain company -- it was an agent of prairie farmers that was empowered to market wheat and barley on their behalf. Western grain farmers' beneficial ownership[2] of the grain extended from farm gate to end use customer.

The CWB's single desk authority allowed it to organize sales and shipments of grain efficiently, serve all areas and farmers equitably and fairly, and consistently provide customers with product meeting their specifications. The CWB could segment[3] the market to obtain premium pricing, and would then return blending benefits[4] to the producers. The CWB built Canada's reputation as the world's premier source of high quality wheat and provided prairie farmers with guaranteed access to markets.

From 1998 until December 2011, ten of the CWB's 15 Directors were farmer-elected; the remaining five were appointed by the federal government. All prairie farmers who were actual producers who grew wheat, oats, barley, rye, flaxseed, and/or canola were eligible to vote and to run for the elected positions. The legislation that destroyed the single-desk authority, the Marketing Freedom for Grain Farmers Act, eliminated the farmer-elected directors and mandated the government-appointed directors to turn the CWB into a private company or liquidate it by the end of 2017. The new CWB is not independent; it is subject to final control by the Minister of Agriculture and Minister of Finance, yet the new legislation declares that it is not a Crown corporation.

The 70-year-old marketing institution, created through democratic processes and designed to serve farmers' interests, is now tasked with reshaping itself into a member of the species it was originally intended to displace: a for-profit grain company that extracts wealth from farmers for the benefit of private shareholders. The measure of its success is no longer the near 100% return of the value of sales to the farmers who produced the grain, but the margin – the difference between the prices paid to farmers when purchasing grain and the price obtained from end-users when selling it. The new CWB is now simply another middle-man.

Dismantling Public Accountability – the Hidden Financial Reports

The government-appointed CWB directors have been at the helm since December 2011, and have been operating the entity as a grain company since August 1, 2012. Each year, the CWB is required to provide its audited financial statements to Parliament. The 2012-13 report was due on March 31, 2014.

It was not tabled in Parliament as required by law, and after persistent inquiries from farmers and journalists were deflected and rebuffed by both the CWB and the Minister of Agriculture, the report finally surfaced in September 2014 – minus all financial information. Only the notes to the audited statement were released, and instead of being tabled in the House of Commons, the report had been submitted to the Parliamentary clerk.

The drafters of the “Marketing Freedom” Act had inserted a new clause under the CWB’s reporting duties that allows the Minister to withhold information if he believes it could harm the CWB’s commercial position. While the former single-desk CWB was fully transparent, the new CWB entity is cloaked in secrecy, ostensibly for business reasons. How the CWB used its government guarantee on financing, the 349 million public dollars allocated in 2012[5] or farmer money – the contingency fund[6] that had reached over $145 million by July 31, 2012 -- is all being hidden. Public accountability has been dismantled along with the single desk.

The single desk CWB fully covered its operating costs, obtained premium prices for Canadian wheat in export markets, managed risks, returned nearly 100% of the crop’s value to farmers annually and prudently invested in assets that built its capacity to serve prairie grain farmers effectively. The CWB was not subsidized by tax dollars. The single desk CWB was a house that farmers built. Now that the demolition team has finished its work, the next step is to polish the rubble to make it attractive to an investment buyer.

Reshaping the CWB into a For-Profit Grain Company Behind Closed Doors

The government-appointed CWB directors plan to privatize it before the 2017 deadline. The process is, of course, being carried out behind closed doors. The widely reported initiative of the Farmers of North America (a private business owned by James Mann of Saskatoon)[7] seeking to purchase the CWB’s assets has drawn attention to the shortened timelines. Non-disclosure agreements mean that details of the bidding process are being kept secret. Absent a public tendering process, it has been necessary to seek out information from reliable third parties with varying degrees of access to relevant information. We have been able to discern the following:

- The government does not recognize any farmer equity in the CWB other than the “Farmer Trust” accounts initiated after August 1, 2012 for farmers that deliver grain to the CWB.
- The transaction is being handled by a third party, likely a large accounting firm.
- The government has set undisclosed criteria for a successful bid. These criteria may include investment that will add to the Canadian grain handling infrastructure.
- The dollar amount of the bid/proposed investment may not be an important factor.
- The new entity is to be re-branded.
- There is no disclosure of timelines.
- There is no disclosure of companies involved in bidding.
- No money will change hands. The government denies owning the CWB and denies any claim to ownership by prairie farmers whose grain sales over 70 years provided the wealth that built all aspects of the CWB’s assets (facilities and expertise). Thus, the CWB will sell itself, with the successful bidder keeping both the money used to purchase the CWB and the CWB’s assets.
- The “sale” of the CWB will require approval by the Minister of Agriculture.

We do know that in January 2014 the federal government issued a tender to accounting firms to assess the value of the CWB’s assets in the event of liquidation.[8] This information could also be used to evaluate proposals from companies bidding on privatization. It also begs the question – if the CWB has no owner other than itself and it were to be liquidated instead of privatized – who would cash the cheque?

What has been lost?

The most important asset of the CWB was its single desk authority, gone as of December 16, 2011. Since 2012, other key assets have been stripped: most significantly, over 75% of the Board's personnel -- people who understood Canada's grain markets and production, had relationships with customers and end-users and who embodied the full range of expertise required for operations and management. The CWB has also lost access to high volumes of high quality grain, as farmers have little reason to deliver grain to the new CWB, and many of those who try have been penalized by competing companies when they have tried to do so. The CWB's international reputation for supplying quality-assured grain on time and on budget has suffered, with premium Asian customers publically expressing concerns about the Canadian grain trade's recent performance.

At privatization, the CWB will lose its AAA credit rating due to end of the government guarantee, making financing more expensive for the CWB itself and eliminating its ability to collect the difference between the old AAA credit rating and the commercial rate the CWB charged end-use customers. The government-appointed directors have purchased Mission Terminal at Thunder Bay, two inland grain terminals[9] in Saskatchewan, and are building four inland terminals in Saskatchewan and Manitoba. The annual audit's financial information, which is being kept secret, might have shed light on where the money to build and buy these facilities came from, as well as revealing the financial impact of CWB assets already liquidated or destroyed.

"Solving" the logistics problems

The apparent criterion requiring the successful bidder to invest in new infrastructure is a government attempt to change the channel by "solving" the logistics problems that crippled the grain system in 2013-14 with more and/or larger terminals. **In fact, the bottlenecks were not caused by lack of capacity or transportation problems, but were due to the lack of coordination resulting from the demise of the single desk.** Competition among both grain companies and farmers, each trying to be first in line, results in a stampede: the door is blocked and nobody gets through. Orderly marketing made efficient use of existing facilities, allowed for planned and prudent expansion, and provided assurance that everyone would get their turn and nobody would lose on price or access by waiting.

Furthermore, 2013-14's bottlenecks benefited the grain companies immensely, as they were able to use them to justify charging a wide basis[10], thus de-valuing farmers' grain. The government's push to increase inland terminal capacity by dangling a carrot in the form of the CWB's assets as a reward would worsen farmers' position. Additional storage capacity, when it is under the control of the grain companies instead of farmers, provides a "holding tank" for grain and functions the same way meat packers' captive supply does for the beef industry – by depressing prices to the producer. The ability to store larger quantities of grain will increase a grain company's buffer between farmers in the countryside and its end-use customers, creating room and time for it to increase its margin by buying as low as possible, then controlling the outward supply to maximize its selling price. The legislation to privatize the CWB might be better named the Marketing Freedom for Grain Companies Act.

Smoothing the way for increased foreign ownership of Canada's grain system

While the FNA offers members who pay annual access fees a service by providing generic farm inputs at discounted prices, it has recently entered a new arena, seeking investors to finance the purchase of the CWB's physical assets. It has been promoting this initiative by suggesting that if they buy limited partnership shares in an FNA-led company, farmers will profit from the privatized CWB.[11] There is a strong implication – in media reports, more than in actual FNA material - that farmer-investor ownership would also mean control of the company. However, securities regulations exclude limited partnership shareholders from any role in decision-making – that is the purview of the general partner.[12] Securities regulations also require limited partnership shares to be offered only to "accredited investors" – those with multi-million dollar net worth and/or consistent six-figure incomes.[13] While some farmers would be eligible to invest, so would non-farmers, and there is no requirement for a general partner to disclose the ownership of limited partnership shares.

Whether farmers or not, investors in the new limited partnership will not be entitled to any role in the operation of the company for which the FNA is the successful bidder. Although several media outlets have mistakenly reported that the FNA is a co-operative, it is, in fact, a sole proprietorship. (See footnote 7) "Members" of FNA have no vote; they simply obtain a discount on the products FNA sells. Regardless of how the FNA – or for that matter, any other company that takes over the CWB's assets – is structured, it will function as a profit-seeking private corporation. It will maximize returns to its own shareholders – not to farmers – even if some of its investors happen to also own farms and use the company's services.

Even with additional infrastructure, CWB's existing and planned physical assets do not add up to the full range of facilities needed to run a successful grain company. Like other grain companies, it would be subject to the same logistical problems created when the single desk's coordinating role was eliminated. Lacking west coast terminal[14] access, it would be restricted to shipping through Thunder Bay during ice-free periods on the Great Lakes. **In the most probable scenario, a privatized and rebranded CWB would operate at a loss for a few years, followed by either bankruptcy or a fire sale to a larger company.** One of the "big three" currently operating in Canada (Swiss-based Glencore, owner of Viterra; US privately-owned Cargill; and privately-owned Richardson) or a new entry (e.g. China's COFCO or Japan's Marubeni, both increasing their international holdings in the grain trade), would no doubt be happy to add discount-priced former CWB facilities to its holdings. This is a familiar trajectory for farmers who invested in the industrialization of the hog sector following the elimination of single desk provincial hog marketing boards in the late 1990s. After investing their savings they watched local mega-barns go into bankruptcy, sold to larger companies at cents on the dollar by creditors.

As private companies, Richardson and Cargill are not subject to stock market pressure to maintain high share prices, and can thus withstand periods of low profitability if necessary to gain market share and control. Glencore, while not private, is one of the world's largest corporations, involved in mining and oil as well as agriculture. It owns one-third of Canada's grain handling capacity and dominates South Australia's grain system, but does not depend on grain for its viability. Marubeni acquired the US grain company, Gavilon, in 2012 and recently entered a joint venture with Archer Daniels Midland to expand their port facilities in Portland, Oregon and Kalama, Washington[15]. COFCO is a state-owned food company that also has responsibilities regarding China's food security and domestic prices[16], enabling it to accept reduced short-term commercial profitability in return for long-term political stability.

Far from gaining control in the grain industry, farmers who invested in FNA's proposed company would almost surely see their investment dollars used to help grain companies enhance their profits at the expense of farm gate prices and smooth the way for increased foreign ownership of the Canadian grain system. Even if the FNA is able to raise enough money to "buy" the CWB assets, the federal government may refuse its bid without revealing the size of competing bids, then claim that farmers were not sufficiently interested in owning the privatized company.

The federal government unilaterally destroyed the single desk system that served the farmers and all of Canada very well. The FNA's initiative, whether intentionally or not, has created a political shield that shifts farmers' attention from the economic disaster that Agriculture Minister Gerry Ritz has set in motion. Private investment for private gain is no solution to the drastic loss of wealth and annual income all prairie grain farmers now face. The public relations value of the FNA's grain company initiative, perhaps coincidentally, serves both the federal government's and grain companies' interests very well. But farmers' interests? Not so much.

Endnotes:

[1] *An Act to reorganize the Canadian Wheat Board and to make consequential and related amendments to certain Acts*, short title "*Marketing Freedom for Grain Farmers Act*"
http://www.parl.gc.ca/LegisInfo/BillDetails.aspx?Language=E&Mode=1&billId=5169698

[2] A *beneficial owner* is entitled to the benefit of owning the property in question even though the title to that property is in another's name, usually in situations where the other acts as an intermediary (e.g. an agent, trustee) on behalf of the beneficial owner.

[3] Because the single desk CWB controlled all wheat and barley exports from the prairies, it was able to offer specific grades of grain according to customer specifications to each customer (*market segment*) and obtain higher prices for farmers as a result.

[4] To meet customer specifications, different qualities (grades) of grain may be mixed to obtain the highest market value possible, or the *blending benefit* for a given supply.

[5] *News Release - Harper Government Delivers Support for a Strong, Viable, Voluntary CWB*, June 28, 2012

[6] See note 22 on page 63 of the *CWB Annual Report*, 2011-12.
http://www.cwb.ca/_uploads/documents/annualreports/CWB2011-12annualreport.pdf

[7] Entity No: 101085879, sole proprietorship doing business under the names "Farmers of North America" and "FNA". *Profile report*, Saskatchewan Corporate Registry, Information Services Corporation of Saskatchewan.

[8] *Tender Notice: A complete and thorough assessment and analysis of the Canadian Wheat Board's (CWB) assets and liabilities (01B68-13-0120)*, https://buyandsell.gc.ca/procurement-data/tender-notice/PW-14-00581379?order=title_en&sort=asc

[9] *Inland terminals* are regionally located high-volume grain storage and shipping points situated on the prairies.

[10] *Basis* is the difference between a futures market price for a commodity and its local cash price. Basis levels are the prerogative of the grain buyer and are not subject to government regulation.

[11] FNA's website says: "We must move quickly to ensure farmers can become majority owners in a major grain handling company, capture margins up the value chain, and inject badly needed competition into this industry."
http://fna.ca/grain/information-statement/

[12] In Lehndorff, Justice Farley of the Ontario Court wrote: "... The limited partners leave the running of the business to the general partner and in that respect the care, custody and the maintenance of the property, assets and undertaking of the limited partnership in which the limited partners and the general partner hold an interest."
http://www.duhaime.org/LegalDictionary/L/LimitedPartnership.aspx

[13] The FNA is seeking non-binding commitments from accredited investors that meet the following financial requirements: an individual who, either alone or with a spouse, beneficially owns financial assets having an aggregate realizable value that before taxes, but net of any related liabilities, exceeds $1,000,000; an individual whose net income before taxes exceeded $200,000 in each of the two most recent calendar years or whose net income before taxes combined with that of a spouse exceeded $300,000 in each of the two most recent calendar years and who, in either case, reasonably expects to exceed that net income level in the current calendar year; individual who, either alone or with a spouse, has net assets of at least $5,000,000; a person, other than an individual or investment fund, that has net assets of at least $5,000,000 as shown on its most recently prepared financial statements; a person in respect of which all of the owners of interests, direct, indirect or beneficial, except the voting securities required by law to be owned by directors, are persons that are described in 1, 2, 3 or 4 above or are otherwise accredited investors (within the meaning of securities legislation). http://fna.ca/grain/commitment-letter/

[14] The Port of Vancouver is fully built up – there is no possibility of adding another grain terminal there. The only grain terminal at Prince Rupert is jointly owned by Cargill, Richardson and Viterra.

[15] *Marubeni and ADM Bolster Export Joint Venture in U.S. Pacific Northwest*, October 1, 2014. https://www.marubeni.com/news/2014/release/00040.html

[16] *Implementing the country's macroeconomic control policies*, COFCO website. http://www.cofco.com/en/csr/20546.html