



National Farmers Union

Submission to the

Canadian Grain Commission

Consultation on

**Inspection and Weighing Requirements for
Grain Exported to the United States**

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Introduction

The National Farmers Union welcomes this opportunity to respond to the Canadian Grain Commission's request for consultations on its proposals to change the regulations regarding official inspection and weighing requirements for exports of grain to the United States.

The National Farmers Union is a nation-wide, democratic, direct-membership organization of farm families. Our members produce a wide variety of commodities, including grains for domestic and export consumption. Consequently, a large percentage of our membership, particularly in western Canada, will be directly affected by any change in the regulations affecting weighing and inspection of grain exports.

The members of the NFU strongly advocate retention and strengthening of CGC official weighing and inspection of all grains destined for export, whether that grain is exported to the United States or any other destination, and regardless of whether the grain is shipped from primary elevators on the prairies, transfer elevators, or terminal elevators at tidewater.

The proposal by the CGC would exempt vessels destined for direct export to the United States from requirements for official inspection and weighing. In its background paper, the CGC states that it has received "several requests" to implement such an exemption. However, it does not reveal which parties have made such requests. Certainly farmers have not been asking for regulatory changes designed to alter the role of the Canadian Grain Commission.

Farmers have consistently spoken out against moves that weaken the ability of the Canadian Grain Commission to protect farmers' interests.

Grain dealers, grain companies, brokers and shipping companies which transport bulk grain shipments by water will obviously benefit substantially from a change in regulations designed to reduce their costs and maximize their profitability. It stands to reason that the requests for such changes originated with these vested interests.

In a marketplace dominated by a relative handful of very large corporations with a tremendous amount of financial muscle, farmers are finding themselves increasingly at a disadvantage. Since the mid-1990s, the CGC has steadily moved from a regulatory body which enforces grain quality standards in the interests of producers and the public at large, to an arms-length monitoring agency whose primary aim is to facilitate the commercial interests of corporations involved in the grain trade.

Historical context

The *Canada Grain Act (CGA)*, passed in 1912, established the Canadian Grain Commission (CGC). Section 13 of the CGA stipulates that the CGC is obliged, first and foremost, to operate “in the interests of grain producers” in the establishment and maintenance of standards of quality for Canadian grain, and “to regulate grain handling in Canada to ensure a dependable commodity for domestic and export markets.”

As the wording of this Section indicates, the CGC was clearly established as the farmers’ watchdog on the grain industry. That objective has been reaffirmed numerous times in the past nine decades.

In 1987, on the occasion of the CGC’s 75th anniversary, then CGC Chief Commissioner G.G. Leith wrote in the introduction to the Commission’s official history book: “The establishment of the Act and the Board (of Grain Commissioners) was the response of the Government of Canada to demands by western producers for regulation of the grain gathering and transportation system... Then, as now, the Commission’s purpose was to protect farmers’ interests and, through the *Canada Grain Act*, to provide a legislative framework for a fast-growing grain industry. Active lobbying by farmers had made the government well aware of the practices which needed remedy.”¹

While Leith went on to note that the CGC legislation allowed for “settlement of disputes” between farmers and grain companies, it is clear the primary purpose of the CGC was to act in the interests of farmers. The author of the CGC official history book, J. Blanchard, acknowledges the implementation of the CGA was a direct response to abuse of market power by grain companies and railways: “There can be no doubt that there were abuses in western Canada – this was inevitable in a situation where the railroad and the grain trade held all the cards and the farmer held none.”²

The situation which existed nearly a century ago is not unlike the context farmers find themselves in now. Four grain companies and two railways dominate the Canadian grain handling and transportation system,³ and it is only through a strong regulatory framework provided by the CGA and the ability of the farmers’ marketing agency, the Canadian Wheat Board, to intervene on farmers’ behalf, that the abuses of the early 1900s are kept in check.

¹ A History of the Canadian Grain Commission 1912-1987 by J. Blanchard. Published by the Canadian Grain Commission, 1987. Minister of Supply and Services Canada

² *ibid.*

³ The Farm Crisis and Corporate Profits, National Farmers Union, 2005

The assertion that the CGA was implemented to protect farmers' interests is confirmed when the Act is compared with federal legislation passed in other countries. "Federal legislation in the US... was not passed until 1917 and then in a form designed to satisfy the powerful grain trade lobby...Further afield, in Argentina, grain producers had no opportunity at all to make themselves heard. The vast tenant farms were tied into a system controlled by the railroads and large grain companies – a system which worked only to their advantage."⁴

Western Canadian farmers of the early 1900s lobbied hard to have an Act passed which would regulate the grading system. Examples abound of farmers being cheated on both grade and weight. In response, they provided hard evidence to the government to prove their grievances were justified.

In 1899, a Royal Commission appointed by Parliament heard testimony from western farmers. Its report documented the injustices in the system and provided the framework for the *Manitoba Grain Act*, which in turn provided the foundation for the *Canada Grain Act* of 1912. One of the commissioners was Charles Castle, who later became the official Warehouse Commissioner under the *Manitoba Grain Act*. In August, 1909, Castle undertook an audit of the terminal elevators at the lakehead. "It was discovered that the stocks and shipments of No. 1 Northern, in the case of two terminals, exceeded receipts by over one million bushels. There were corresponding shortages in lower grades and some of the surplus was no doubt due to not cleaning grain to the level of dockage required. Thus it was proven that grain was mixed to promote grades, as every western producer had suspected. The companies in question were prosecuted and fines were levied."⁵

The annual weigh-up of grain in store at terminal elevators thus served to ensure accountability on the part of grain companies.⁶ The principle of official weighing and inspection contributed heavily to Canada's enviable reputation for consistently accurate weights and high quality of grain shipments over the past century.

The principle of government having a direct role in grain inspection is well-established in Canada. Over a century ago, when grain inspection was carried out on a private contract basis with individual grain companies, the system was over-burdened with conflict and inefficiencies. In 1901, a Royal Commission established to look into problems with grain inspection in Montreal, concluded:

"...in some fifty-two instances during the past year, in which the inspection made would not warrant the inspector in certifying the grade expected or demanded, his grading was not accepted, and no certificate was issued, and the parcels were either sold by sample, or certificates procured from some other sources, no fees being paid the inspector in any such cases, nor any surveys demanded to settle who was in the wrong. It does not seem to

⁴ A History of the Canadian Grain Commission 1912-1987. Canadian Grain Commission

⁵ Ibid, page 17.

⁶ "The annual weigh-up was established as effective tool for discovering wrongdoing." Ibid, page 50

the commissioners proper that the trade should have it in their power to withhold the fee when the certificate is not to their liking nor on the other hand, should there be any incentive on the part of the inspector to cultivate business. The commissioners therefore consider that instead of by fee, the inspectors and all officers or employees connected with grain inspection should be paid by salary.”⁷

Returning to an inspection system based on self-policing by grain companies and contracting with third-party private inspectors is a step backward, and will undermine Canada’s reputation as a reliable supplier of high-quality grains for export.

Before the rise of the farmer-owned co-operative elevator companies, four global grain companies controlled the global market. In western Canada, they operated through “front” companies – line elevator companies set up to trade on the Winnipeg Grain Exchange. Their overriding influence and market power was reduced as a result of the rise of the prairie Wheat Pools, and the implementation of the CGA. But over the past decade, the four major farmer-owned co-operative grain handling companies have disappeared, and farmers are once again facing a situation where they are confronted by a shrinking number of huge, US-based transnational corporations. Today, the top five grain companies control close to 80% of the global grain trade.⁸

History, and the experience of farmers in other countries, has shown that private, for-profit grain companies and/or their agents cannot be trusted to provide unbiased, fair and accurate measurement of grade and weight. While it may be true that the regulatory framework imposed on these grain companies under the *Canada Grain Act* increases their operating expenses, the benefits to farmers, and their customers, more than justify the regulations.

Since 1912, farmers and the nation as a whole have benefited from the fair and independent assessment of grade and dockage, licensed and bonded elevators, a transparent and regulated grain exchange, and the right of farmers to load their own producer cars. These innovations have allowed Canada to gain and maintain world market share based on high-quality grains.

As an internal CGC document noted in 1992: “The Canadian grading system was established to provide form and structure to the standards of quality that have been developed for Canadian grain. Division of quality is structured to offer the producers the opportunity to receive a price for their grain relative to its quality and to enable our customers to obtain the same quality on a consistent basis. We then endeavour to link those objectives by facilitating the transitory process from farm to vessel or farm to processor. Ultimately, a certificate is issued guaranteeing the quality attested.”⁹

⁷ Royal Commission on the Inspection of Grain at Montreal, 1901, page 43. Quoted in *A History of the Canadian Grain Commission: 1912 to 1987*, by J. Blanchard. Page 20.

⁸ Presentation by Adrian Measner, Canadian Wheat Board CEO, at a symposium in Regina sponsored by the NFU and the University of Regina, February 24, 2006. Reported in the *Union Farmer Quarterly*, Summer, 2006.

⁹ Internal Review of the Regulation Administered by the Canadian Grain Commission. Canadian Grain Commission, July, 1992

For the CGC to fulfill the quality control mandate of the CGA, representative sampling of grain is key. Representative samples, particularly those obtained through inward inspection, are essential for official inspection certificates – the final guarantee for farmers – and customers - of quality, weight and grade.

Eliminating official inspection and weighing for exports of grains to the US will increase the pressure from grain companies to have the requirement eliminated for exports to other destinations as well. The CGC’s stated commitment to “consistency” establishes a precedent for accommodating the grain companies’ demands for further exemptions under the CGA.

Official Inspection and Weighing of grain exports to the US

In 1995, the *Canada Grain Regulations* were amended to eliminate the requirement for official inspection and weighing of grain transported to the US from licensed primary and transfer elevators. These amendments resulted from intense lobbying by the Western Grain Elevator Association. However, the regulations still stipulated that official inspection and weighing was necessary at port facilities.

Since 1997, when the Grain Commission proposed curtailing inward inspection at ports (again, in response to pressure from the Western Grain Elevator Association), the NFU has been the most active farm organization in Canada in studying and evaluating CGC programs and operations and in making recommendations to improve and strengthen the CGC.

In its background paper, entitled “Consultation on US Export Policy – Questions and Answers, and dated January 15, 2009, the Canadian Grain Commission states that it “seeks a coherent and consistent policy applicable to all exports of Canadian grain to the United States.”

However, it is clear that the stated goal of “consistency” is merely a smokescreen designed to hide the real objective. If “consistency” was truly the goal, both options would be examined equally. However, the option of strengthening official inspection and weighing to once again include primary and transfer elevators is not even considered.

In the background paper, the CGC states: “stakeholders have expressed concern to the CGC that inconsistent requirements represent a competitive disadvantage for one conveyance type in relation to another.”

However, it is well established that costs associated with grain shipments, including transportation, tariffs and handling charges, are all eventually passed back to the producer. There is little evidence to suggest that farmers whose grain is shipped by rail from inland elevators to the United States receive any higher returns than those whose grain is shipped from port terminals. Therefore, the argument that a “competitive

disadvantage” afflicts port terminal operators such as those along the St. Lawrence Seaway, is without serious merit.

The CGC provides statistics that show that 90% of total grain shipments from all of Canada to the US are conveyed by truck or rail, and that only 10% of the shipments are by lake or ocean-going vessel.¹⁰ The rationale for the proposed change appears to be that because most of the grain is already not subject to CGC official inspection and weighing, the impact on the overall system would be negligible.

However, the effect of removing official CGC inspection and weighing at the terminal elevators would be far more significant than those numbers would indicate. The CGC issues official certificates indicating grade and dockage of grain subject to official inspection. These official certificates provide legal protection to the farmer by virtue of their signifying official grade and weight of grain shipped. They also provide a guarantee to the final customer regarding grade and quality of the grain they are buying from Canada. In cases where the CGC was not involved in weighing or inspecting the grain shipped, the farmer therefore does not have the legal protection of the CGC certificate of official inspection. Farmers who mistakenly assume the CGC’s role and responsibility have not changed, will only discover after the fact that they are left unprotected.

The advantages of CGC official inspection

Inward inspection involves taking official samples of grain at terminal and transfer elevators to determine grade and dockage and to determine financial compensation to be credited to the shipper. Inward inspection achieves three important outcomes:

1. it supports Canada’s grain quality and quality assurance systems;
2. it protects the integrity of grain transactions; and
3. it supports producer protection.

Eliminating CGC inspection and weighing activities will undercut these three important broad outcomes, and, therefore, will have a significant negative impact on producers.

Inward inspection ensures that:

- The identity of the grain is established before commingling;
- The identity of the grain is preserved so that the sample will be available to resolve disputes or facilitate the appeal process;
- Substantive and valuable statistical information is available to: a) establish the basis for warehouse receipts; b) identify current stock positions; c) facilitate future audit processes; and d) predict cargo quality prior to shipment.
- Grain is collected to allow for future reviews of grain grades and specifications.
- Final grade assigned by the CGC can be checked against the grade initially assigned by the elevator manager to ensure consistency in accuracy, and to reduce

¹⁰ CGC Chief Commissioner Elwin Hermanson, statement made during a conference call with grain industry stakeholders, January 22, 2009.

- the incidence of penalties imposed by the Canadian Wheat Board (CWB) for “missed grades;
- The presence of illegal or ineligible varieties is detected before these varieties enter the system.
 - CGC-approved automatic sampling systems are monitored.
 - Railway freight rates are based on CGC-monitored weights.

These benefits are of primary importance to farmers, who understand the necessity of a strong CGC, which operates on their behalf.

Again, Canada’s farmers have not advocated any weakening of the CGC regulatory role, nor have they called for cuts to the CGC’s mandate or its resources.

Indeed, the NFU, on behalf of family farmers, has consistently called for a strengthening of the Grain Commission’s watchdog function, and tougher enforcement of regulations for grain companies.

CGC role as industry regulator, not facilitator

The NFU strongly believes the CGC must reaffirm and strengthen its mandate as industry regulator – protecting farmers’ interests and ensuring fairness in the system. To this end, we recommend the CGC retain and strengthen the current system of inspection at port terminals. They NFU also rejects any suggestion that inward inspection be optional or that grain sampling and/or grain inspection be delegated to grain companies themselves or “accredited” private service providers.

As noted earlier, the grain inspection system in Canada in the late 1800s relied on inspectors who graded grain samples submitted by private companies on a contract basis. If the grade was unacceptable to the company, the inspector was not paid. Inspectors who provided favourable grades to companies were more likely to get paid. It was a system that provided ample opportunity for error and graft. It was only after inspection and weighing were put under the mandate of the CGC that the system was able to implement consistently high professional standards.

This latter point is critical given the CGC’s continued moves toward accrediting private inspection services. A CGC background paper, released in June, 2008, outlines the Accredited and Certified Container Sampling Programs. These programs involve voluntary “accredited” and “certified” container sampling programs, with sampling being performed either by accredited third party contractors or by grain companies themselves. In 2006-07, approximately 3 million tonnes of grains were shipped using containers. It is expected that the crop year 2007-08 will see an increase in the tonnage of grain shipments by containers.¹¹ Because containers, under the CGA, are not required to be officially inspected by the CGC, these proposed voluntary programs are being

¹¹ Jim Smolik, Canadian Grain Commission Assistant Chief Commissioner, statement made during a conference call with grain industry stakeholders, January 22, 2009

implemented as a way of alleviating customers' concerns that they will actually receive the grain they pay for.

The Accredited Container Sampling Program (ACSP) would see the CGC "accredit" a third party service provider. This accredited service provider would then be obliged to follow CGC protocols regarding sampling, and give official grade on that sample to the CGC. The CGC would, in turn, audit and monitor that third party service provider to ensure it meets the CGC requirements. The accredited third party service provider would also be required to not have any vested interest in the container that is being shipped.

Under the second program, known as Certified Container Sampling Program (CCSP), the CGC simply "certifies" that a private grain company has done its own sampling and sent the sample to the CGC. The sample is retained by the CGC but is not considered an official sample. The CGC trains staff people from grain companies, such as Viterra or Cargill, in how to take grain samples using specified equipment and recognized CGC protocols, but the grain company uses its own staff to do the actual sampling and also employs its own quality management system for the process.

Under this proposed program, the "accredited" sample receives the same status as an "official" CGC sample that was taken by a CGC employee. Under the "certified" sample protocol, the sample would not be given the same status as an "official" CGC sample.

The CGC indicated in June, 2008, that it was seeking input on these proposed programs from grain companies. No mention is made that input was sought from producers or producer organizations.

One of the largest private inspection, verification, testing and certification companies in the world is SGS Group, which operates over 1000 offices and laboratories and employs over 43,000 people around the world. One of its clients is Cargill, the dominant player in the global grain trade. If Canada's grain inspection services were contracted out, SGS would be well-positioned to capture the business.

The use of terms such as "certified" and "accredited" in place of "official" to refer to samples taken by grain company employees or third party service providers are confusing at best, and deceitful at worst. Farmers may mistakenly assume that they will have the same protection regarding grade and quality for a "certified" sample of their grain taken by a Cargill employee, or an "accredited" sample taken by an SGS employee, as they would for an "official" sample taken by a CGC employee.

If the proposed programs are adopted on a widespread basis, the monetary benefits to the private grain trade of this system are readily apparent. The financial liability to farmers is less immediately obvious, but is nonetheless a major concern.

The CGC, through its various functions including inward inspection, constitutes a high value investment for farmers. The CGC is mandated to operate in the public interest, not in the interest of private shareholders who are seeking a profit.

The high quality of Canadian grain, for which the CGC is primarily responsible, puts hundreds of millions of dollars in farmers' pockets every year. Weakening the CGC's ability to perform any of its obligations – and particularly CGC official inspection – is an ill-conceived approach that will end up reducing farmers' returns.

Given the fact that realized net farm incomes continue to remain at record low levels, it is unconscionable that a policy of further reducing those incomes is being seriously considered.

Financial implications of phasing out CGC inward inspection

It is true that structural changes in the grain handling and transportation system have had an impact on CGC operations. Over the past 45 years, the number of primary elevators has fallen from over 5000 to 375,¹² and average grain receipts at port terminals have dropped by about 20 percent since the early 1990s. Average storage capacity at primary elevators has gone from 2000 tonnes to over 10,000 tonnes, with some facilities capable of storing 100,000 tonnes.¹³ But this should not be used as justification for phasing out mandatory inward inspection.

The NFU estimates that cost savings resulting from centralizing inward inspections would be extremely small – roughly \$2.5 million annually – or one quarter of a penny per bushel¹⁴. This small saving would not come close to offsetting the potential costs of missing problem carloads of grain and subsequently mixing those missed loads into the inventories held in storage at port terminals.

The NFU believes that mandatory, immediate, on-site inward inspection by CGC inspectors provides substantial benefits to the system. It allows inspectors to “catch” contaminated, off-condition or incorrectly-represented carloads while they are being emptied, weighed, and elevated, and before they are mixed with large quantities of other grain. Even if contaminated or off-spec grain is binned, current inward inspection procedures allow problems to be spotted and isolated almost immediately.

¹² In addition to the decline in elevators, the number of grain delivery points in western Canada has declined to 274. Monitoring the Grain Handling and Transportation System, 1st Quarter, 2007-08 Crop Year, Quorum Corporation, June 2008,

¹³ Letter from NFU President Stewart Wells to Hon. Bob Speller, Minister of Agriculture and Agri-Food, April 5, 2004.

¹⁴ NFU Submission to the Minister of Agriculture and Agri-Food on the Canadian Grain Commission's Program and Governance Reviews, Ottawa, ON, March 23, 1999. This document is included at the end of this brief as Appendix A.

The maintenance of the current system of inward inspection is also of vital importance to the farmers' marketing body, the Canadian Wheat Board. The CWB needs to know exactly what type and grade of grain is being delivered into a given terminal at a given time. Inward inspection is also of critical importance to producer car shippers, because the Canada Grain Act says specifically that they will have official weighing and inspection at unload. All these producer-based organizations rely for their continued business success on the information collected from inward inspection and weighing services performed by the CGC.

If the mandatory inspection and weighing functions of the CGC were eliminated or revised, the impact on the financial and business interests of individual farmers, their producer-car loading facilities, and their marketing agency, the Canadian Wheat Board, would be massive – and also entirely negative. There would be no benefit to farmers in reducing or phasing out the CGC's current role. In fact, farmers would be fundamentally worse off under such a regime – just as they were a century ago before the Canada Grain Act was passed by Parliament.

In the opinion of the National Farmers Union, producers' rights would not be protected under either the Accredited Container Sampling Program nor the Certified Container Sampling Program. These proposed programs would also not ensure the integrity of grain transactions would be preserved.

Likewise, eliminating the official inspection and weighing requirements for terminal elevators at port would further jeopardize Canada's grain quality guarantees and protection for producers and customers.

Funding for the CGC is dependent on an annual grant from the Parliament of Canada, and the perennial problem of deficits is one which needs to be addressed realistically within the mandate of the CGC. That is, it must be done in such a way that the interests of farmers are protected. The CGC deficit – which in recent years has amounted to approximately \$10 million annually – is in some ways a result of the CGC management's own choices.¹⁵ Since 1991, the CGC had frozen its fees. In contrast, over that same period from 1991 to 2002, grain companies increased their handling and elevation tariffs by 44%.¹⁶ Had the CGC increased its charges at just one-half the rate that grain companies increased theirs, the CGC would have a surplus.

Seen another way, a \$10 million CGC deficit equals approximately 43 cents per tonne. This is just one penny per bushel. For a strong and effective CGC farmers will be willing to pay the penny.

Of course farmers want to control costs. And of course we want to maximize the effectiveness and efficiency of the agencies that protect us, such as the CGC. In the current climate, however, it seems far more prudent for farmers to pay an extra penny per

¹⁵ NFU Submission to the Canadian Grain Commission Review Panel, Winnipeg, MB, June 30, 2002

¹⁶ Average tariff, Saskatchewan Agriculture and Food, Stat Facts

bushel than to risk falling victim to industry-driven cuts to the CGC that may result in farmers losing much more than a penny.

The NFU recommends that the CGC increase its fees to cover its projected deficit. Further, CGC fees should be adjusted upward each year, as needed to cover its expenses at a rate not exceeding the increase in the average elevator tariff.

Conclusion

In recent years, there has been a steady process of undermining the CGC's role and mandate. In the 1990s, a series of internal recommendations by the CGC management called for greater deregulation of the grain quality system. A review in 2006 by Meyers Norris Penny examined the costs and benefits of the requirement, under the *Canada Grain Act*, of inspection and weighing of every rail car arriving at a terminal or transfer elevator. This inspection and weighing was to be carried out by CGC personnel, who took samples to establish grade, dockage, moisture and protein and to check for contamination or infestation. Also in that year, an overall review of the CGC and the *Canada Grain Act* was undertaken by Compas Consultants. The Compas report was used as the basis for Bill C-39, a bill which proposed a number of amendments to the *Canada Grain Act*. Bill C-39 died on the order paper in the fall of 2008, but it is widely expected similar legislation will be introduced in the future by the current Harper government.

In all these reviews, the NFU has consistently emphasized the need to retain a strong regulatory mechanism that protects the interests of Canadian farmers and the quality standards of the Canadian grain system.

Grain handling companies have been very outspoken in their opposition to the requirement that every rail car arriving at a terminal or transfer elevator be weighed and inspected. In fact, they have been pressing for decades to have it eliminated. They claim it "represents an unnecessary and costly intrusion into their business and say it should be made optional."¹⁷ These companies have also lobbied hard to have the CGC move away from its role as a regulator of the grain industry, which works on behalf of farmers, to a passive service provider which provides grading, weighting and inspection services to grain companies for a specified fee.

The National Farmers Union believes that moving the CGC from a regulator role to a service provider role is very short-sighted and would go against the public interest. Farmers in western Canada fought long and hard to have strong regulations created for the betterment of the grain industry, and those regulations have paid huge dividends to all players in the system, including grain companies, farmers, and the nation as a whole. We strongly recommend that the CGC retain its role as the farmers' watchdog in the system; and that mandatory inward inspection continue to be a function of the CGC.

¹⁷ "CGC review criticized", Western Producer, March 23, 2006

As noted earlier, farmers have not called for changes to inward inspection. Nor will they benefit from any changes, which will amount to between a tenth of a penny and a quarter of a penny per bushel in savings for the grain companies.¹⁸ There is also no evidence to suggest that grain companies will feel compelled to pass such small savings on to farmers. Farmers, therefore, will pay twice for the weakening of the CGC in the area of inward inspection: the first through the loss of current benefits; and the second through the refusal of grain companies to pass on any potential savings to farmers.

All of which is respectfully submitted

By the National Farmers Union

¹⁸ NFU Submission to the Canadian Grain Commission Review Panel, Winnipeg, MB, June 30, 2002