801.1(b)
802.52
802.64

Verne, B. Michael

From: [redacted]
Sent: Thursday, August 12, 2004 4:02 PM
To: Verne, B. Michael
Cc: Johnson, Janice C.; [redacted]
Subject: HSR questions

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(422 KB)

Mike,

This e-mail is a follow-up to a number of conversations/e-mail exchanges we had in early June regarding the Canada Pension Plan (the "Plan") and Canada Pension Plan Investment Board (the "Investment Board"), the company that invests funds not needed by the Plan to pay current pensions. We seek your advice in determining who "controls" the Investment Board for purposes of the Hart-Scott-Rodino Act of 1976, as amended ("HSR"). Janice Johnson suggested that we lay out our questions in an e-mail.

By way of background:

1. The Investment Board was incorporated as a Federal crown corporation by an Act of Parliament, pursuant to which, the Investment Board issued 10 shares of the Investment Board (the "Shares") to the Minister of Finance (the "Minister") to be held on behalf of Her Majesty in right of Canada, the Canadian government. There are no shares of the Investment Board other than the Shares. It is not clear whether the Shares are "voting securities" for HSR purposes. The Act of Parliament gives the Canadian government the right to appoint all the directors of the Investment Board (see #2 below), but it does not specifically link this right to the Shares.

2. Pursuant to the Act of Parliament, the Governor in Council (the equivalent of the U.S. Federal Cabinet) is empowered to appoint all of the directors of the Investment Board on the recommendation of the Minister. (We assume, for HSR purposes, that the Governor in Council is viewed as an extension of the Canadian government.)

3. The Investment Board invests in capital markets funds that are transferred to it from the Plan which are not needed by the Plan to pay current pensions. The Investment Board is required, on 30 days' notice from the Minister, to transfer funds to the Plan if the Minister considers the transfer is necessary to meet any payment obligation of the Plan. The Investment Board is not expected to be required to contribute funds to the Plan to help pay pensions until 2021.

4. The Investment Board's governing statute provides that no statute relating to the insolvency or winding-up of any corporation

applies to the Investment Board and in no case shall the affairs of the Investment Board be wound up unless Parliament so provides.

5. We attach some further background information about the Investment Board and the Plan below which may be helpful in understanding the relationship between them. This information was downloaded from the Investment Board's website on August 11, 2004.

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Based on the foregoing facts, it is unclear to us who "controls" the Investment Board for HSR purposes. Our HSR analysis is set forth below:

A. We believe that the Canadian government controls the Investment Board for purposes of HSR because (i) it holds 50% or more of all outstanding securities of the Investment Board and/or (ii) it has the sole right to appoint all of the directors of the Investment Board . — AGREE

B. However, if the Shares are not considered voting securities, then the Plan could "control" the Investment Board under HSR because it is entitled to all of the net profit of the Investment Board . — NO - THIS IS A CORPORATION.

If the Investment Board is determined to be controlled by the Canadian government, please confirm that acquisitions or sales by the Investment Board (or its subsidiaries) of assets located within Canada or voting securities of an issuer organized in Canada would be exempt under Section 802.52 of the HSR regulations. — YES

We also discussed the applicability of the "institutional investor" exemption under Section 802.64 and you advised me that Canada public pension plans qualify as institutional investors under 802.64(a)(10), however, the exemption would not be applicable because the Plan is not directly acquiring the voting securities. If it is determined that the Plan "controls" the Investment Board, would the exemption still be inapplicable because the Plan is not "directly" acquiring the voting securities?

— NO - BOTH THE INVESTMENT BOARD & THE PLAN ARE CONTROLLED BY THE CANADIAN GOVERNMENT, BUT THE PLAN DOES NOT CONTROL THE BOARD.

If you have any questions please do not hesitate to contact [redacted] at [redacted] or me at [redacted]. We look forward to hearing from you.

Regards

[redacted]

B. [illegible]
8/16/04

Tel: [redacted]
Fax: [redacted]

[redacted]

CPP INVESTMENT BOARD

Who We Are

The CPP Investment Board is a professional investment management organization based in Toronto. Our purpose is to invest funds received from the Canada Pension Plan in a way that maximizes returns. Income from the money that we invest today will be used by the Canada Pension Plan to help pay the pensions of working Canadians who will begin retiring 17 years from now.

We were incorporated as a federal Crown corporation by an Act of Parliament in December 1997 and made our first investment in March 1999.

Our team is small and highly experienced. We are committed to remaining small because we believe it is the best way to deliver good performance while keeping costs under control.

Our mandate and objectives

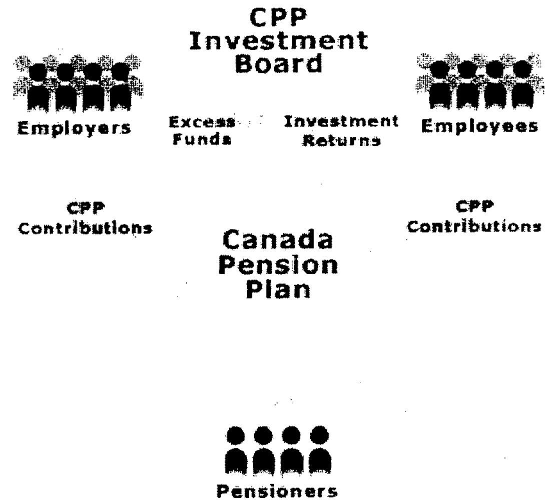
Our mandate is set out in our legislation:

- To invest in the best interests of CPP contributors and beneficiaries, and
- To maximize long-term investment returns without undue risk of loss, taking into account the factors that may affect the funding of the Canada Pension Plan and its ability to meet its financial obligations.

The CPP Investment Board cannot conduct any business or activity that is inconsistent with these objectives.

We are also committed to telling our story and sharing information with Canadians so that they understand the role that we play in ensuring that the Canada Pension Plan will have more than sufficient resources to pay public pensions in the future.

How we're funded



Our independence

We operate independently of the Canada Pension Plan and at arm's length from the federal and provincial governments which were jointly responsible for the creation of the Plan. Independence from governments in making investment decisions is critical to our success and public confidence in our organization.

Role of government

The role of government is limited. The federal finance minister, in consultation with the participating provinces:

- Appoints our directors,
- Reviews our legislation and regulations every three years as part of the review of the Canada Pension Plan, and
- Is required to initiate a special examination of our financial and management controls, information systems and management practices, at least once every six years.

We send our quarterly financial statements and annual report to all finance ministers. Our annual report must be tabled in the House of Commons each year.

Changes to our legislation and regulations can only be made with the support of the federal government and two-thirds of the participating provinces representing two-thirds of the population.

Accountable to beneficiaries and the public

We are accountable to the 16 million Canadians who contribute to or benefit from the Canada Pension Plan and to the general public. We keep the public informed through public meetings that must be held once every two years in every participating province, to review our annual report. We also post information and important developments on our website and issue news releases to the media.

We are a small, cost effective corporation

In the traditional corporate model, most implementation and support functions are performed by employees who are an integral part of the core organizational structure. If we had chosen this model, we would have had to build an elaborate organization with a large staff.

Instead, we chose to build a small, cost effective corporation with a small team of senior executives responsible for developing investment and operating strategies, and then accessing and leveraging external expertise to help us manage our assets and increase their long-term value. This approach ensures broad exposure to ideas, deal flow and service providers through partner-like relationships at home and abroad, while leaving open the option of developing staff expertise to implement components of our strategy wherever and whenever equal or better results can be achieved internally at lower cost.

Whether executed internally or externally, our executives are responsible and accountable for all aspects of our investment and business performance as well as compliance and control. Our team includes experienced professionals in research and risk management, public market investments, private market investments, communications and stakeholder relations, finance and operations, and legal and corporate secretariat matters.

We believe our corporate model focuses our energies on value-added activities, provides access to specialized skills and resources, offers flexibility in choosing required skills and capabilities, generates potentially better results at less cost, and provides risk management and diversification benefits. In other words, our organization is a strategic think-tank that takes full tactical advantage of the talents already flourishing in the competitive marketplace to implement our strategies.

Our operating costs

Controlling costs and getting value for the expenses we incur is key to maximizing net investment returns. Our investment and administrative expenses are included in our annual report. For the year ended March 31, 2003, these expenses represent seven basis points or roughly seven cents per $100 of invested assets (a standard industry measurement).

Our investment costs include such expenses as custodial services, investment fund management fees and consulting costs. These expenses will increase as the assets under management grow.

Administrative costs are tightly controlled by the board and management and include salaries and wages, occupancy, information technology, office supplies and equipment, directors' remuneration and other miscellaneous overhead expenditures.

Our fiscal year ends March 31 and our annual report is issued in May.

Our Team Our Governance Our Policies

CPP INVESTMENT BOARD

Why We Exist

Why We Exist

The CPP Investment Board was conceived as a result of a public review of the Canada Pension Plan in 1996. The review was commissioned by federal and provincial finance ministers to ensure that the Plan would be affordable and available to Canadians today and for generations to come.

In 1996 the Canada Pension Plan lacked sufficient assets to meet long-term obligations. As a result of the public review, in 1997, the finance ministers agreed to raise contribution rates to levels that will generate funds in excess of those required to pay pensions until at least 2021.

To ensure that the funds will earn maximum returns until they are needed, the ministers created the CPP Investment Board, an independent investment corporation, to invest the excess contributions and the proceeds from maturing bonds held by the Canada Pension Plan. In this way, the Canada Pension Plan will continue to be affordable and will, in the view of the finance ministers, be sufficiently funded to pay the pensions of Canadians in the future.

To fully understand why the CPP Investment Board exists it is useful to understand the history of the Canada Pension Plan and the outcome of the 1996 public review.

Please enter your search criteria here

Search

Canada Pension Plan | Our History | Our Legislation | Our Regulations

The Canada Pension Plan was established in 1966 to provide all working Canadians with retirement income and financial assistance to their families in the event of death or disability. The annual contribution rate was set at 3.6 per cent of earnings. The Plan, administered on behalf of all participating provinces by the federal government, replaced a portion of the worker's pre-retirement earnings with a guaranteed pension.

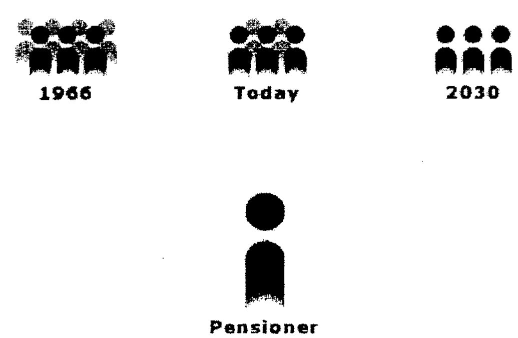
The Canada Pension Plan was designed as a "pay-as-you-go" rather than a "fully funded" pension plan. This meant that each generation paid the pensions of the previous generation.

The Canada Pension Plan worked well for 30 years. For most of that time, substantially more money flowed in than was paid out.

By the mid-nineties, however, despite an increase in the contribution rate to six per cent of earnings in 1996, projections indicated that changing demographics and increasing life expectancy of Canadians meant that more money was being paid out in benefits than was being collected. As a result, the Canada Pension Plan was headed for serious trouble.

In the sixteenth actuarial report on the Canada Pension Plan, the Chief Actuary predicted that the Canada Pension Plan's reserve fund, the equivalent of two years of benefits, would be depleted by 2015. He estimated that future generations would have to pay 14.2 per cent of contributory earnings to pay the pensions of retired Canadians.

A Maturing Pension Plan



The ratio of CPP contributors to beneficiaries has decreased from 7:1 in 1966 to 5:1 in 2002. By 2030, there will be only three CPP contributors to support every pensioner.

Canada Pension Plan Review

The impending pension crisis sparked an extensive review by the federal and provincial governments in 1996. Public hearings were held across Canada along with a series of meetings with federal and provincial finance ministers, who are ultimately responsible for the Canada Pension Plan.

On February 9, 1996, the federal, provincial and territorial governments released a joint information paper on the Canada Pension Plan entitled *An Information Paper for Consultations on the Canada Pension Plan*. This paper formed the basis for consultation with the Canadian public.

On March 28, 1996, David Walker, then Member of Parliament for Winnipeg-North Centre, was appointed chief federal representative for the public consultations. One Member of Parliament, and at least one elected representative from the respective provincial or territorial governments, joined Mr. Walker for each public meeting.

Public consultation began on April 15, 1996. More than 270 Canadians made formal presentations during 33 sessions held in 18 cities. In addition, the CPP Secretariat received 140 written submissions and 6,000 inquiries or comments were logged to the 1-800 information line.

Quebec, which has its own plan, the Quebec Pension Plan, conducted its own public consultations within the province in parallel with the consultations on the Canada Pension Plan.

Canada Pension Plan Improvements

As a result of the review and input received during the consultation process, several changes were implemented to put the Canada Pension Plan on firmer financial footing and build greater assets for the future.

- Contribution rates were increased from six per cent in 1997 to 9.9 per cent of maximum pensionable earnings by 2003
- Improvements were made to the Canada Pension Plan administration to lower operating costs
- The CPP reserve fund target was increased from two to five years of benefits
- A new funding level goal was established. The Plan is expected to be 20 per cent funded (that is, CPP assets will equal 20 per cent of the liabilities - or pension obligations) by 2017
- Pension plan statements were scheduled to be issued annually to all contributors and beneficiaries
- The Canada Pension Plan Investment Board, an independent investment organization separate from the Canada Pension Plan, was established to invest excess CPP funds in a diversified portfolio of securities, and
- The federal and provincial finance ministers agreed to review the Canada Pension Plan and the CPP Investment Board every three years instead of every five years.

These changes, outlined in a paper titled *Securing the Canada Pension Plan: Agreement on Proposed Changes to the Canada Pension Plan*, were approved by Parliament in December 1997 and received the formal approval of the participating provinces soon after.

Changes to the schedule of contribution rates were made effective January 1, 1998 and the CPP Investment Board began operations in April 1998.

The changes made to the Canada Pension Plan and the creation of the CPP Investment Board will ensure that the Canada Pension Plan is affordable to future generations and can be sustained in the face of an aging population, increasing longevity, and the retirement of the baby-boom generation.