



**CPP  
INVESTMENT  
BOARD**

Canada Pension Plan Investment Board  
One Queen Street East, Suite 2600  
PO Box 101  
Toronto, Ontario M5C 2W5  
Toll Free 1 866-557-9510  
Telephone: 416-868-4075  
Web site [www.cppib.ca](http://www.cppib.ca)

June 24, 2009

The Honourable James M. Flaherty  
Minister of Finance  
Minister's Office  
21st Floor, East Tower  
140 O'Connor Street  
Ottawa, Ontario K1A 0G5

Dear Minister:

In response to your letter of June 2, 2009, our Board of Directors has assessed the CPP Investment Board ("CPPIB") incentive compensation framework against the principles and practices recently recommended by the Financial Stability Forum ("FSF") and endorsed by the G-20 leaders.

The Board of Directors met yesterday, reviewed a report from the Board's independent compensation consultant confirming their view that the CPPIB's compensation practices are consistent with the principles and practices recommended by the FSF, and approved the submission of the attached report to all ten finance ministers, the federal and provincial stewards of the CPPIB to whom we are accountable.

Based upon our assessment, we can assure you that the CPPIB compensation framework, policies and practices clearly meet and in many cases exceed the standards set out in the G-20 Principles on Compensation in Financial Services. Indeed, we believe that CPPIB's compensation structure, which has been in place for over three years, meets best practice standards not just for institutional investors, but for financial institutions and public companies globally.

The CPPIB compensation structure overseen by the Board of Directors also reflects our organization's long-term goals and its strong risk management culture designed to invest the \$105.5 billion CPP Fund for decades and generations on behalf of 17 million Canadians.

As you know, the Financial Stability Forum specified nine compensation practices underlying the three principles you cited in your letter. We have analyzed CPPIB's policies and procedures relative to each of the FSF's recommended practices and include a detailed assessment as an Appendix to this letter. In addition, for each of the three overarching FSF principles I have provided below a summary of that more detailed analysis.

**1. Firms' boards of directors [to] play an active role in the design, operation, and evaluation of compensation schemes:**

- CPPIB's overall board and governance structure meets the highest standards of independence, expertise and involvement. Its governance model is admired globally and is referenced by bodies such as The World Bank and the OECD as one for other countries to emulate.
- The CPPIB Board of Directors is ultimately responsible for and approves the design, operation and evaluation of CPPIB's compensation structure.
- CPPIB's Board of Directors has created a committee of the Board, the Human Resources and Compensation Committee (HRCC), with responsibility for recommending the design of the compensation system to the Board and for monitoring its ongoing operation. Members of the HRCC have the requisite compensation and risk management expertise.
- The HRCC has engaged a compensation consultant, Hugessen Consulting Inc. ("HCI"), to provide an expert and independent assessment of the design and operations of the CPPIB compensation structure. As detailed in the Appendix, during fiscal 2009 the HRCC with HCI's assistance reviewed and evaluated all aspects of the design and operation of the compensation structure.
- The Board of Directors, upon the recommendation of the HRCC, approves all elements of both the overall compensation structure and the specific compensation awards for the CEO and all Senior Officers.

**2. Compensation arrangements, including bonuses, [to] properly reflect risk and the timing and composition of payments to be sensitive to the time horizon of risks. Payment should not be finalized over short periods where risks are realized over long periods:**

- CPPIB operates within a Risk Return Accountability Framework which is established by the Board of Directors. The compensation system flows directly from this framework to ensure that management is not encouraged to take excessive investment risk.
- The Board of Directors is firmly committed to a pay-for-performance philosophy that directly links investment related compensation to value-added investment returns. In this respect, CPPIB evaluates actual investment performance against market index related benchmarks that are approved by the HRCC and that recognize the specific inherent risks of investment strategies including, where appropriate, the degree of leverage used, specific geographic and industry risks, horizon of investment and associated liquidity risk. More qualitative risks such as reputational, regulatory, legal and tax are also taken into consideration in our investment processes.

- The portion of compensation related to investment performance is based upon performance over rolling four-year periods. We believe this longer time period not only meets the FSF principle noted above but also places CPPIB at the forefront of current best practices for financial institutions. Moreover, this four-year timeframe is consistent with our long term investment mandate and a sufficient and appropriate match for the risks inherent in our investment programs.
- No investment performance based incentive payouts will be made to management unless actual returns for the CPP Fund or individual investment programs exceed benchmark returns as calculated over rolling four-year periods. At the overall CPP Fund level, excess returns over the most recent measurement period have totaled \$5.3 billion. Long term performance incentives are also adjusted by the absolute returns of the total CPP Fund over the performance period further reinforcing the linkage between incentive amounts and CPP Fund performance.
- To ensure that all investment performance elements of compensation are calculated correctly, CPPIB's external auditors, Deloitte & Touche, audit the calculations of actual and benchmark results and provide a report to the HRCC confirming accuracy.

**3. Firms [to] publicly disclose clear, comprehensive, and timely information about compensation. Stakeholders, including shareholders, should be adequately informed on a timely basis on compensation policies to exercise effective monitoring**

- CPPIB published a comprehensive, 15 page Compensation Discussion and Analysis as a component of our 2009 Annual Report. We believe that this extensive disclosure not only meets the FSF's stated principle, but also represents a best practice standard for comparable organizations to CPPIB within Canada and globally.

The HRCC has also asked our independent, external compensation consultant, HCI to review our assessment of our practices relative to the G-20 principles; HCI concurs with our conclusions.

The Board of Directors takes its responsibility to ensure that CPPIB acts in the best interest of the 17 million Canadian contributors and beneficiaries of the CPP very seriously. We appreciate this opportunity to explain, in detail, our transparent compensation and related governance structures which are consistent with our long term goals as an investor.

Please let me know if you require any further information.

Yours respectfully,



Robert M. Astley  
Chair, Board of Directors  
Canada Pension Plan Investment Board

**Financial Stability Forum Principles for Sound Compensation Practices**  
**CPP Investment Board's (CPPIB) Compensation Practices**

<b>Principle</b>	<b>Practice</b>
<b>1.</b>	<p><b><i>The firm's board of directors must actively oversee the compensation system's design and operation.</i></b></p> <ul style="list-style-type: none"> <li>• CPPIB's Board of Directors has created a committee of the board, the Human Resources and Compensation Committee ("HRCC"), which has responsibility for determining the design of the compensation system and its ongoing operations. Members of the HRCC have the requisite compensation and risk management expertise.</li> <li>• The HRCC has engaged an independent advisor, Hugessen Consulting Inc (HCI), to provide advice directly to the committee on the appropriateness and competitiveness of CPPIB's compensation program.</li> <li>• The full Board of Directors is ultimately responsible for approving the compensation framework for the CPPIB upon the recommendation of the HRCC, as well as all elements of compensation for CPPIB's CEO and Senior Officers.</li> </ul>
<b>2.</b>	<p><b><i>The firm's board of directors must monitor and review the compensation system to ensure the system operates as intended.</i></b></p> <ul style="list-style-type: none"> <li>• The CPPIB's Board of Directors has assigned primary responsibility for monitoring and reviewing the compensation system to the HRCC. The HRCC's Terms of Reference set out the requirements and schedule for regularly monitoring the compensation program to ensure it is operating as intended at all levels of the organization.</li> <li>• As confirmed in CPPIB's 2009 Annual Report, amongst other activities, the HRCC during fiscal 2009: <ul style="list-style-type: none"> <li>▪ Reviewed and reconfirmed the overall compensation framework, including the compensation principles and objectives, pay-for-performance linkages, comparator groups and competitive positioning.</li> <li>▪ Reviewed, approved and where appropriate recommended for board approval the value added benchmarks and performance targets for incentive compensation.</li> <li>▪ Benchmarked compensation structures and levels for officers.</li> <li>▪ For the CEO and Senior Officers, reviewed performance and recommended to the Board salary levels and incentive compensation payouts.</li> <li>▪ For non-officers, approved the aggregate salary increase budget and recommended to the Board aggregate incentive compensation payouts.</li> <li>▪ Modeled compensation scenarios that illustrate the impact of various future performance outcomes on compensation.</li> <li>▪ Undertook, with HCI's support, a review of executive compensation trends and practices.</li> </ul> </li> <li>• To ensure that all investment performance elements of compensation are calculated accurately, the HRCC engaged CPPIB's external auditors, Deloitte &amp; Touche, to audit the calculations of actual and benchmark results and provide a report to the committee confirming accuracy.</li> </ul>

**Financial Stability Forum Principles for Sound Compensation Practices**  
**CPP Investment Board's (CPPIB) Compensation Practices**

Principle	Practice
3.	<p><i>Staff engaged in financial and risk control must be independent, have appropriate authority and be compensated in a manner that is independent of the business areas they oversee and commensurate with their key role in the firm.</i></p> <ul style="list-style-type: none"> <li>• Employees responsible for financial and risk controls reside in CPPIB's Finance or Treasury, Risk, Operations, Technology departments. Both departments report and operate independently from all investment departments. Their roles and responsibilities for financial control and risk management are documented and well understood.</li> <li>• The Senior Officers responsible for financial and risk controls (specifically the Chief Financial Officer and the Chief Operating Officer) report directly to the CEO. They are also members of CPPIB's Investment Planning Committee ("IPC") and provide the IPC with financial, valuation and risk assessments that are independent of the investment departments.</li> <li>• A significant component of the incentive compensation for finance and risk management staff is based upon achievement of specific department and role based objectives. Any investment performance component of their compensation is based upon the total CPP Fund performance over a four-year period rather than any investment department results they may oversee.</li> </ul>
4.	<p><i>Compensation must be adjusted for all types of risk.</i></p> <ul style="list-style-type: none"> <li>• CPPIB operates within a Risk Return Accountability Framework which is approved by the Board of Directors. This framework articulates the appropriate level of investment risk CPPIB's management can employ in order to fulfill the organization's mandate.</li> <li>• CPPIB establishes benchmarks and performance targets that recognize the specific inherent risks of investment strategies employed and assets acquired. For example, benchmarks for private assets (typically the most difficult to assess given a lack of availability of market pricing) are adjusted to reflect the degree of leverage used, specific geographic and industry risks, horizon of investment and associated liquidity risk. More qualitative risks such as reputational, regulatory, legal and tax are also taken into account in our investment processes.</li> <li>• Where appropriate, as in the case of investments in public markets for example, approved compensation targets and thresholds are determined according to active risk expectations and allocations within a risk budgeting process carried out annually.</li> <li>• A portion of the incentive compensation of all employees, including investment professionals, is tied to the total CPP Fund performance measured as value-added versus the benchmark Reference Portfolio. This approach assists in aligning interests, supports our Total Portfolio Approach to risk management and reinforces that investment decisions should be made for the long term benefit of the overall CPP Fund.</li> </ul>

**Financial Stability Forum Principles for Sound Compensation Practices**  
**CPP Investment Board's (CPPIB) Compensation Practices**

Principle	Practice
<b>5.</b>	<b><i>Compensation outcomes should be symmetric with risk outcomes.</i></b>
	<ul style="list-style-type: none"> <li>• Investment performance incentive compensation, which includes incentive compensation under both the Short-Term and Long-Term Incentive Plans as described in the annual report, is based upon actual investment returns relative to returns for benchmarks that have been approved by the HRCC. In the case of the total CPP Fund, the benchmark is the return for the CPP Reference Portfolio which is described in the 2009 Annual Report. For individual investment programs, benchmarks are selected based upon their relevance to the nature of the investing activity.</li> <li>• No investment performance incentive payments will be made unless actual investment performance exceeds benchmark returns calculated over rolling four-year periods.</li> <li>• Investment performance multipliers are calculated for each year of these rolling four-year periods. Individual year multipliers can be positive or negative and are symmetric above and below a predetermined target multiplier level.</li> <li>• In addition to being symmetric with risk outcomes, multipliers are also subject to symmetric caps and floors. In conjunction with the four-year measurement periods, these act to moderate the impact of any single year's performance on incentive compensation payments.</li> <li>• Long term incentive payouts are also adjusted by the absolute returns of the total fund over the four year average period, further reinforcing the linkage between incentive amounts and actual CPP Fund performance over time.</li> </ul>
<b>6.</b>	<b><i>Compensation payout schedules must be sensitive to the time horizon of risks.</i></b>
	<ul style="list-style-type: none"> <li>• Investment performance incentive compensation is measured over four-year periods to ensure payouts reflect sustained levels of investment performance.</li> <li>• We believe this longer period for calculating incentive payments balances our long term mandate with a reasonable accountability timeframe, encourages CPPIB to make sound, long term investments, and sufficiently reflects the time horizon of risks inherent in most of our investment programs.</li> </ul>

**Financial Stability Forum Principles for Sound Compensation Practices**  
**CPP Investment Board's (CPPIB) Compensation Practices**

Principle	Practice
7.	<p><b><i>The mix of cash, equity and other forms of compensation must be consistent with risk alignment.</i></b></p> <ul style="list-style-type: none"> <li>• The specific mix of compensation within CPPIB varies by role.</li> <li>• Investment professionals have a significant portion of their compensation determined by four-year investment results to ensure alignment with the risk and returns of their investment decisions.</li> <li>• The investment performance incentive compensation for senior investment professionals is more heavily weighted to total CPP Fund performance than less senior roles. This ensures that individuals involved with investment strategy, policy and approval responsibilities are incentivized to make decisions in the context of what is best for the overall CPP Fund.</li> <li>• Individual performance elements of incentive compensation are much more significant for non-investment roles within CPPIB to reflect the nature of their responsibilities; any investment performance component of incentive compensation is based entirely upon total CPP Fund performance over rolling four-year periods.</li> </ul>
8.	<p><b><i>Supervisory review of compensation practices must be rigorous and sustained, and deficiencies must be addressed promptly with supervisory action.</i></b></p> <ul style="list-style-type: none"> <li>• The HRCC and the Board of Directors provide primary supervisory oversight of CPPIB's compensation practices.</li> <li>• Some of the activities the HRCC undertook in fiscal 2009 were listed in the response to Principle 2; a more complete description is contained in the Compensation Discussion and Analysis section of our 2009 Annual Report.</li> <li>• As previously noted, the HRCC has engaged a compensation consultant, HCI, to provide them with an independent, third party confirmation that CPPIB's compensation practices meet rigorous standards based upon their experience.</li> <li>• As a shareholder in a large number of companies, CPPIB encourages the adoption of rigorous compensation practices through our Proxy Voting Principles and Guidelines. In all relevant instances, our own practices meet or exceed these guidelines.</li> </ul>
9.	<p><b><i>Firms must disclose clear, comprehensive and timely information about their compensation practices to facilitate constructive engagement by all stakeholders</i></b></p> <ul style="list-style-type: none"> <li>• We believe that the extensive disclosure that CPPIB provides about our compensation practices through the Compensation Discussion and Analysis section of the 2009 Annual Report is not only a best practice standard for comparable organizations to CPPIB within Canada, but meets the high standards of disclosure we expect of the public companies in which we invest.</li> </ul>