

# INDUSTRY

By Jeff Sanford

To contribute, call (416) 764-3829, fax (416) 764-3934 or e-mail [asharratt@rmpublishing.com](mailto:asharratt@rmpublishing.com)

## Caisse reports biggest investment loss in 37-year history

**“HAD WE KEPT OUR ASSET MIX CLOSE TO THE REFERENCE PORTFOLIO, WE WOULD HAVE LOST WHAT THE AVERAGE CANADIAN PENSION FUND HAS BEEN LOSING.”**

**—HENRI-PAUL ROUSSEAU,  
CHAIRMAN AND CHIEF  
EXECUTIVE OFFICER,  
CAISSE DE DÉPÔT ET  
PLACEMENT DU QUÉBEC**

The Caisse de dépôt et placement du Québec reported the largest annual investment loss in its 37-year history when it announced last month that its net assets declined 9.6% in value in 2002, a loss of \$8.6 billion for the fund.

Much of the loss can be traced to the Caisse's investments in the technology, media and telecommunications (TMT) sector. The pension fund also says its investment in a convergence play by Quebecor Media Inc. also contributed to the loss. In a press release, Caisse chairman and chief executive officer, Henri-Paul Rousseau was quoted as saying, “The Caisse, like a large number of financial institutions, was involved in the speculative TMT bubble in the last years of the century. The Caisse stands out, however, because of its late entry into the sector and the scope and illiquid nature of its investments.”

But Rousseau also suggested that meddling by “centralized operations” in the strategies of various Caisse fund managers led to an extra loss of \$600 million. “Had we kept our asset mix close to the reference portfolio, we would have lost what the average Canadian pension fund has been losing, which is 4.5%, 5%.”

At the press conference last month announcing the loss, Rousseau focused on his restructuring plan. To that end, a new “integrated risk management committee,” a group of senior executives whose aim is to minimize similar losses in the future, has been created. The Caisse also unveiled a group of governance recommendations it will submit to the Québec

government. These include splitting the CEO and chairman functions, having the board appoint the CEO and removing executive duties from the chairperson's role. The chairperson, however, would be responsible for forming a committee to appoint directors to the board with a majority of independent members.

“We want to have an independent board of directors,” says Rousseau. “That would mean that there will be a better equilibrium between accountability and transparency.”

As of Dec. 31, 2002, the Caisse managed \$77.7 billion in net depositor assets.

## Teachers' still beats benchmark

The Ontario Teachers' Pension Plan also reported its 2002 investment performance numbers last month. The results, although negative, could have been worse had the fund not limited its equity exposure last year.

The fund had an investment loss of \$1.4 billion or 2% of its value, compared to its benchmark of -4.8%. “We were able to beat all of our benchmarks in the major asset classes and beat our overall benchmark by 3%,” says Lee Fullerton, a spokesperson for Teachers' in Toronto. “We think that's an accomplishment.”

Inflation-sensitive and fixed-income investments performed well last year, returning 13.2% and 8.6% respectively. The loss came from the equity side of the portfolio, which returned -14.1% overall and -7.7% in Canadian equities. Teachers' says it limited the damage to the portfolio by trimming its equity holdings in 2002.

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“The big reason we were able to do as well as we did was a decision made early in the year to change our asset mix,” says Fullerton. Teachers’ has been reducing its exposure to equities for three years. But the plan aggressively vacated the asset class by lowering its equity holdings from 60% of the total portfolio to 49% by the end of the year.

“We took a big jump this year. We didn’t have confidence in the stock market so we took a big risk. But that decision saved the fund about \$1 billion,” says Fullerton.

At the end of 2002, net assets were \$66.2 billion, down from \$69.5 billion in 2001.

## Farm co-operative members launch suit against plan

Members of a multi-employer pension plan covering 26 Ontario farm co-operatives have launched a class action suit against the trustees, custodians and investment manager of the plan, which they claim are renegeing on their pension promise.

The 2,300 current members of the Participating Co-operatives of Ontario Trusteed Pension Plan launched the class action in March after the pensions of some members were cut and others were notified that they had been overpaid.

“It is a pretty sad situation,” says Ari Kaplan, a lawyer with the Toronto law firm Koskie Minsky, which is handling the suit. “Employees and pensioners are angry, they feel betrayed. Some have been members for 20 or 30 years and they’ve been counting on this money. Now they’re being told to expect 50 cents on the dollar.”

The plan, which was the subject of a recent internal Financial Services Commission of Ontario (FSCO) report, has suffered disastrous investment losses. According to the FSCO report—which examined such practices as the use of derivative contracts by the investment manager—there is only \$64 million left in the fund to meet \$120 million in liabilities.

Kaplan points out that what is remarkable about this case is that many of the losses occurred at the height of the late-1990s equity boom—arguably the largest market boom in history. “I’ve never seen a fund go from surplus to 59% funding in just a couple of years. But what sets this case apart from other situations where funds have lost money—which all funds have done lately—is the time period we’re talking about,” says Kaplan. “The suit specifically refers to a time between 1997 and 2000 when funds were realizing gains of 10% to 20% at least, and this fund was losing money. Our suit alleges that someone fell asleep at the wheel and that those charged with managing the plan acted contrary to their fiduciary duty.”

According to Kaplan, plan members are concerned because they may not be eligible for compensation from Ontario’s Pension Benefits Guarantee Fund, which does

not cover multi-employer plans. “In a multi-employer plan, the risk of underfunding shifts to plan members. The only net these plan members have is this class action suit,” says Kaplan.

Koskie Minsky hoped to file a statement of claim by the end of March. But Kaplan hopes that publicity will work to register the seriousness of the case with Canadian plan trustees.

“This is a defined benefit plan—not some group RRSP. For their entire working career these people have been expecting a certain amount in retirement. That’s what a defined benefit plan is all about,” says Kaplan. “The initial responsibility here falls on the shoulders of trustees. If anything, this case will show how important a position that is. When you agree to take on that position it’s a great responsibility.”

## NDP to make pensions an issue in the next Ontario election

The Ontario New Democratic Party is promising to make pensions a key issue in the next provincial election, says an advisor to Howard Hampton, the party’s leader.

“Historically we’ve always been advocates of pension reform,” says Ethan Phillips, the NDP provincial pension advisor. He suggests the focus on pensions is partly the result of the Conservative government’s recent handling of the pension surplus issue. “That isn’t the only issue driving this but certainly we were concerned with the lack of action from the government on that,” says Phillips.

The major reform proposed by the NDP would see pensions indexed to the rate of inflation. According to Phillips, this is something that’s already written into Ontario law but has never come into effect, because no government has come up with the required indexing formula. “This is something that’s already in the pension act. We only lack the formula and we think it’s time to do that and put inflation indexation on the table,” says Phillips.

The formula the NDP is suggesting would see pensions indexed at 75% of the consumer price index (CPI) minus 1%. So if CPI came in at 4% for the year, the index rate would be 75% of 3%, or 2.25%. For plans without a surplus, the NDP is suggesting an alternative formula of 25% of CPI minus 1%.

The NDP would also reduce vesting periods, which currently occur two years after the start of employment. According to Phillips, an NDP government would eliminate the vesting period altogether. “That’s the law in Québec and it’s working fine,” says Phillips.

With respect to surpluses, Phillips said an NDP government would also clarify the rules around surpluses and put employee representatives on pension governance boards. He also confirmed the NDP would plan to write

into law current practices such as employer/plan member negotiation regarding surplus distribution.

An NDP government would also work to expand the number of Ontario employees covered by a pension plan, says Phillips. “Currently, only about 40% of workers are covered by a pension plan. We would establish a royal commission to look at the best way to cover more people and consult with stakeholders on any initiative to increase participation,” says Phillips. “One way to do that would be to make it easier to create multi-employer plans to encourage more small companies to offer a pension plan.”

One final recommendation would be to increase contributions to the Ontario Pension Benefits Guarantee Fund and increase the current guaranteed maximum benefit of \$1,000. “That hasn’t been increased since 1987 and it’s about time it was,” says Phillips.

## Canadian companies reverse hiring expectations

Canadian companies have changed their hiring plans over the winter, according to Mercer Human Resource Consulting’s *Compensation Planning Survey Update, 2003*.

When the survey was conducted in September 2002,

many companies indicated that they were planning to lay off employees. But that attitude seems to have changed, a subsequent survey conducted in January has found.

“I was surprised, but we saw relatively few organizations planning to reduce their headcount. Most are sitting tight,” says Merrillyn Earl, a human resources consultant with Mercer in Toronto.

In September, 20% of companies said they were planning to cut their workforce, a number that dropped to 9% in January. “Many organizations have simply frozen hiring, but aren’t getting rid of people,” says Earl.

In fact, on the upside, 23% of survey respondents said they plan to add more staff, up from the 17% of respondents who indicated they planned to hire more staff in September’s survey.

However, in terms of salary increases, it looks as if employees shouldn’t expect any new money to come their way. The survey suggests the average salary increase will be about 3.3%, a number that will keep pace with inflation but provide no real growth in wages.

According to Earl, that average amount is much lower than the average salary increases of 7% to 8% of seven or eight years ago. “Organizations used to spend what they needed to get the right employee. Now companies are spending only what they are able to,” says Earl. “The

pressure on supply isn't there. It's not like what we saw in information technology (IT) in the late nineties."

According to Earl, above average salary growth will happen in the oil and gas industries (up 3.6%) as well as in the pharmaceutical industry (up 3.8%). Sectors experiencing below average growth include finance and banking (3.0%) and IT (2.7%).

## Canadian institutions step up governance

Canadian institutional investors have stepped up their governance campaign with a flurry of announcements around proxy voting guidelines.

The Toronto-based Canada Pension Plan Investment Board (CPPIB) announced in March it had drafted new standards for boards of directors that will go beyond what is currently required under the voluntary guidelines for listing on the Toronto Stock Exchange. The CPPIB says it will vote against options and instead support direct share ownership by directors and management.

The Investment Counsel Association of Canada (ICAC) in Toronto also released new governance voting guidelines for its members. An industry trade group for investment fund professionals founded in

1952, the association has a membership that manages in excess of \$475 billion in client assets. Until now, it has been fairly quiet in terms of industry activism. But that may be changing, says Keith Douglas, ICAC's executive director.

"This is new for us but I think we want to step up our actions. We certainly want to speak out more on principles," says Douglas. "For obvious reasons our members are interested in corporate governance and this is an attempt to bring in a central standard among members."

The group expects to expand its education efforts and get more involved in distributing information to members. "The majority of our larger member firms are subject to proxy voting and we want to make sure that it is being done," says Douglas.

U.S. pension funds are also pushing on the governance front. Members of the Council of Institutional Investors in Washington, D.C., are considering asking the Securities and Exchange Commission (SEC) to give investors greater power to elect board candidates. Members of the council will vote this month on whether or not to ask the SEC to allow shareholder nominees for director to be listed on corporate proxies. The council is made up of 130 pension funds controlling more than US\$3 trillion in assets.

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