



**Annual Report of the
Southern Boundary Restoration and Enhancement Fund and the
Northern Boundary and Transboundary Rivers Restoration and Enhancement Fund
for the year 2011.**

Introduction

In June of 1999, the United States and Canada reached a comprehensive new agreement (the "1999 Agreement") under the 1985 Pacific Salmon Treaty. Among other provisions, the 1999 Agreement established two bilateral funds: the Northern Boundary and Transboundary Rivers Restoration and Enhancement Fund (Northern Fund); and the Southern Boundary Restoration and Enhancement Fund (Southern Fund). The purpose of the two funds is to support activities in both countries that develop improved information for fishery resource management, rehabilitate and restore marine and freshwater habitat, and enhance wild stock production through low technology techniques. The United States agreed to capitalize the Northern and Southern Funds in the amounts of \$75 million U.S. and \$65 million U.S. respectively. Canada also contributed CAN \$500,000. The 1999 Agreement also established a Northern Fund Committee and a Southern Fund Committee, each comprised of three nationals from each country, to oversee investment of the Funds' assets and make decisions about expenditures on projects. Only the earnings from investments can be spent on projects.

Committee Members

Northern Fund Committee

Canada:

Mel Kotyk
Frank Quinn/Denis D'Amours
Ron Fowler

United States:

Doug Mecum
David Bedford
Jim Bacon

Southern Fund Committee

Canada:

Don Radford
Don Hall
Mike Griswold

United States:

Larry Peck
Larry Rutter
"JP" Olney Patt

Executive Summary

- Total contributed capital (nominal) was \$US 140,065,000 (the equivalent of \$CDN 209,796,000 using the exchange rate at the time the last installment was made). Actual fund asset value at December 31st, 2011 was \$US 174,280,000 or \$CDN 177,243,000.
- Last year was marked by a return of risk as investors grew increasingly concerned about many European economies and the debate about the U.S. fiscal situation. The Fund eked out a small positive return for the year and outperformed the Benchmark by 0.5%.
- The Joint Fund Committees took decisions in 2011 to diversify the investment portfolio into real estate and infrastructure as a risk reduction measure.
- In 2011 the Southern Fund Committee supported a total of 24 projects for U.S. \$1.54 million.
- In 2011 the Northern Fund Committee supported a total of 24 projects for U.S. \$1.73 million.
- U.S. \$2 million was contributed to the Chinook Sentinel Stocks Program in 2011, U.S. \$1 million each from the two Committees. In addition, a second installment of U.S. \$492,500 was paid to the United States in repayment for funds provided by the U.S. government in support of the Sentinel Stocks program in 2009.
- Total Fund project expenditures to date are \$41.6M US, in support of 585 projects, as well as the Sentinel Stocks program.
- Northern and Southern Fund Committee members met jointly once in 2011. In addition, the Northern Fund Committee met three times in separate sessions and the Southern Fund Committee met four times in separate sessions.
- For Canada, Dr. Denis D'Amours replaced Mr. Frank Quinn on the Northern Fund Committee, on an "acting" basis.
- Fund staff assumed administrative responsibility for the Yukon River Panel Restoration and Enhancement Fund.

Investment Review

2011 was marked by a return of risk as investors grew increasingly concerned about a series of global events ranging from the European sovereign debt crisis, to the Middle Eastern revolution, the tsunami in Japan and the debate about the U.S. fiscal situation marked by all-night debates on the debt ceiling. With these concerns about the global economy, interest rates diverged - in the weaker economies, rates rose as investors demanded more return for their willingness to lend. On the other hand, many countries, including Canada, were considered relative safe havens and bond yields fell. This led to strong returns in the Canadian bond market with a one-year gain of 9.7%. On the other hand, equity markets generally declined and the benchmark for global equity markets was down 5.5% (in local currency terms) for the full year. Within those equity markets, the riskier the location, the greater the decline, as evidenced by a drop of 18.4% in the emerging markets index. The Fund eked out a small positive return for the year and outperformed the Benchmark by 0.5%.

The Total Fund return of +4.1% was 0.1% below the benchmark return for the first quarter of 2011, after deducting investment management fees. For the past twelve months, the net of fee performance was below the benchmark return of +13.0% by a slightly larger amount: 1.4%. LSV's relatively weak stock selection outside of North American was influenced by a significant natural disaster in Japan. This was offset by Brandes' sector allocation impact which was positive during the quarter, especially given their relatively large overweight position in the Telecoms sector and absence from the Materials sector.

During the second quarter, the market value of the Total Fund decreased by \$4.2 million, comprised of \$8.0 million in net cash outflows, \$0.7 million in investment income, \$0.5 million in capital gains, and \$2.6 million in currency impact. However, the Total Fund return of +2.0% was 0.4% ahead of the benchmark return for the quarter, after deducting investment management fees. The impact from BlackRock's stock picking for the period was positive with strong picks in the Consumer Staples sector leading the way. Brandes' stock selection in the global portfolio was a negative influence, especially within the Consumer Discretionary sector.

The Fund declined 12.4% in the third quarter of 2011, slightly better than the 12.6% drop in the benchmark much of which can be attributed to events in Europe. Relative results were modest across the board. Brandes added value but this was offset by LSV in equal measure. The bias to bonds over equities added value as bonds significantly outperformed during the quarter.

Equity markets rebounded strongly at the end of 2011, after significant declines in the summer and early fall. Global equities rose 7.8% (in local currency terms) with the U.S. posting even higher returns (+11.8%). This reflected a relative abatement of the crisis in Europe and signs of improvement in the U.S. economy. Bond markets also performed well, with Canadian bonds rising 2.1%. The bond markets continued to believe that interest rates will remain low for the foreseeable future.

Total contributed capital (nominal) was \$US 140,065,000 (the equivalent of \$CDN 209,796,000 using the exchange rate at the time the last installment was made). Actual fund asset value at December 31st, 2011 was \$US 174,280,000 or \$CDN 177,243,000.

Contributed capital and asset value of the individual Funds as of December 31st, 2011 stood as follows:

Contributed Capital		Asset Value	
Northern:	\$US 75,000,000 \$CDN 112,388,000	\$US 95,443,000	\$CDN 97,065,000
Southern:	\$US 65,000,000 \$CDN 97,408,000	\$US 78,837,000	\$CDN 80,178,000

Note #1:

In 2003 a rescission of 0.65% applied to the FY 2003 appropriations reduced the final contribution to the Northern Fund by \$US162,500 and to the Southern Fund by \$US97,500. Thus the actual Contributed Capital is:

Northern: \$US 74,837,500
 Southern: \$US 64,902,500

Note #2:

U.S. Dollar Exchange (noon) rate: per Royal Trust, December 31, 2011	1.017	0.98328
U.S. Dollar Exchange (noon) rate: per Royal Trust, November 30, 2011	1.0197	0.98068
U.S. Dollar Exchange (noon) rate: per Royal Trust, December 31, 2010	0.9946	1.00543

2011 Project Funding

The effects of the 2008/09 global financial crisis and subsequent weak investment climate had a strongly negative effect on Northern and Southern Fund investments. Gradual gains in the Funds' value were realized starting in the second quarter of 2009. By April 2010 when the Fund Committees met to plan their 2011 funding programs, the financial positions of the two Funds had not fully recovered.

The Northern Fund Committee limited its use of available funding to support for a suite of on-going multi-year projects funded by the Northern Fund in the year or years before 2011. There was no Northern Fund Call for Proposals for new projects starting in 2011. The Northern Fund Committee supported a total of 24 on-going projects for U.S. \$1.73 million in 2011.

The Southern Fund Committee forecast a relatively modest amount of funding being available in 2011, so their Call for Proposals was limited to (i) proposals to continue on-going projects (i.e. multi-year projects funded by the SFC in 2010 & earlier) and (ii) new, on-the-ground projects designed to benefit wild stocks of salmon by improving the quality or quantity of their habitat. Ultimately, only six new habitat projects were approved, fewer than had been anticipated. When combined with the suite of 16 on-going projects, the Committee was financially in a position to approve a special request from the Fraser River Panel to fund two hydroacoustic projects to improve the integration of estimates of pink and sockeye passage at the two Fraser sonar sites, Mission and Qualark. In the end the Southern Fund Committee supported a total of 24 projects for U.S. \$1.54 million in 2011.

In the eight years between 2004 and 2011 the Northern Fund has granted U.S. \$20,817,747 to 258 projects. Similarly, between 2004 and 2011 the Southern Fund has granted U.S. \$20,787,466 to 327 projects. Total Fund project expenditures to date are U.S. \$41.6M, in support of 585 projects. The Sentinel Stocks program has been funded in addition to this in the amount of U.S. \$5 million.

Joint Funding Initiatives

In 2008 the Northern and Southern Fund Committees approved motions to support the “Chinook Sentinel Stocks Program” with funds in the amount of \$1M US each, per year, for a period of 5 years beginning in 2009. This commitment was dependent upon Fund performance given that the guarantee of interest income on the Fund in any given year is not assured. In January 2009 the value of the Fund stood at \$127,130M US, some \$13M US below the contributed capital sum. Neither Northern nor Southern Fund was therefore able to support the SSP financially in 2009. Given the unexpected circumstances, the U.S. and Canadian governments stepped in and provided funds to support the Program in its first year. In 2010 the Northern and Southern Funds repaid the Canadian government for their 2009 contribution to the Program in the amount of Can \$500,000. The Funds also paid a first installment to the U.S. government in partial repayment for their 2009 contribution in the amount of \$492,500 US. A second similar installment was paid in 2011 to complete the repayment. Contributions were in the amounts of \$2M US in 2010 and again in 2011 bringing the total contribution to the Sentinel Stocks Program to date to approximately \$5.5M US.

Joint Fund Committee Meetings

The Northern and Southern Fund Committees have agreed that given the congruent nature of their agendas and their decision to combine the funds into a single master account for investment management purposes, and the efficiencies involved with respect to interaction with the fund managers, it was appropriate to meet together as a Joint Fund Committee. The Joint Fund Committee met in person once on November 17th, 2011.

Mr. Chris Kautzky of Aon Hewitt opened the meeting by discussing on-going issues with the Fund’s two active managers Brandes and LSV. He told the Committee that Aon Hewitt still held LSV at their highest manager rating level and advised no changes. With respect to Brandes, Aon Hewitt had been meeting regularly with the firm over the last year to assess their performance. There was something of a divergence in opinion among Aon Hewitt staff who had attended these meetings. Some said the elements that had made Brandes successful 5 years ago were still there, while others said sell. The consensus was that there might be room for improvement in certain process areas, for example the in the way information moves from the analysts to the management committees; and, the effectiveness of the firm’s approach to risk management. Fund Committee members asked if a possible solution might be to stay with Brandes, but adopt a passive management strategy as the Fund had done with BlackRock and it’s US equity portfolio. Mr. Kautzky replied that this was an option, however, the recommendation of Aon Hewitt was that active management of global assets can still add value and minimize risk and that their advice to the Fund Committee would be to continue to hold Brandes.

Mr. Kautzky then gave the Fund Committee a progress report on the alternative asset strategy. He said that the investment sub-committee had conducted interviews in June with three US commercial real estate managers and chosen the firm of Invesco. As this was a new investment vehicle for the Fund and because of the Pacific Salmon Commission’s unique position as an international organization, legal council had been retained to assist with contract negotiations.

These had recently come to a successful conclusion and Mr. Kautzky anticipated the Fund being invested in the first quarter of 2012. In addition, interviews with three commercial real estate managers were due to take place in December.

The Committee then heard presentations from the three investment managers in person. Following the presentations the Committee discussed their next steps.

The Committee felt that the performance of LSV had been acceptable.

Next the Committee considered the performance and outlook for Brandes. While disappointed with their performance over the last four years, the Committee appreciated the stability of the firm's structure, the low turnover in staff, and the consistency of their commitment to the deep value Graham and Dodd investment process. There was some concern that if the world had changed after 2008/09 the Brandes model might be outdated. The consensus was that there was no appetite for rapid change; the Committee would continue to be patient in accordance with Aon Hewitt's advice to "hold"; the Committee were satisfied that Aon Hewitt was doing its due diligence in regularly re-evaluating Brandes and that if at any time the "hold" recommendation were to change to a "sell" recommendation, the Committee would act accordingly.

With respect to BlackRock, the Committee was in agreement that in future, given the passive strategy now adopted with this firm, an annual in-person interview would no longer be necessary and a written report could be submitted.

The last agenda item was a report on the status of the Chinook Sentinel Stocks Program from Sentinel Stocks Committee co-chair Dave Bernard who joined the meeting from Anchorage via conference call. He began by summarizing the financial position of the program and noted that expenditures to date were less than the \$2M per year originally envisioned. He described projects that had met or nearly met their primary objectives on the Fraser (South Thompson and Chilko), Nass, Skeena and Oregon Coast. He also described projects that had yet to achieve a spawning escapement estimate with the desired accuracy and precision for various reasons. These were largely concentrated in Puget Sound and the West Coast of Vancouver Island. He held out the hope that the two-sample study, Coweeman River method, might prove effective in Puget Sound and possibly on the WCVI rivers. He also spoke of a genetic stock identification/coded wire tag approach as possible for WCVI. Some Fund Committee members wondered if either alternative would provide a result more insightful than the current state of knowledge, being that there are very few fish in these systems. While satisfied with the successful results achieved so far by the SSP, the Fund Committee members expressed their concern about Puget Sound and WCVI and questioned the likelihood of these two regions achieving the spawning escapement estimates they sought on time & within the budget allotted. In the meantime, the volume of proposals received in response to the 2011 Call for Proposals for projects starting in 2012 amplified the Committee member's awareness of the impact of this fourth annual SSP disbursement on the Funds annual grant awarding capability.

Northern Fund Committee Meetings

The Northern Fund Committee met three times during 2011.

April 28th, 2011

- Fund performance and Q4 2010 review.
- Alternative asset classes update and discussion.
- The potential for funding in 2011.
- Status of on-going projects in 2011.
- Spending Policy review.
- Target spending amounts based on the most recent financial information.
- Special projects worth considering if a general call be deemed unfeasible.
- Habitat Restoration Technical Committee Co-Chairs Presentation.

September 20th, 2011

- First round selection of project concepts to be invited to proceed to stage two.
- On-going project status and review.

November 17th, 2011

- Financial position and date of record.
- Status of long-term on-going projects.

Southern Fund Committee Meetings

The Southern Fund Committee met four times during 2011.

February 14th, 2011

- Final review and approval of on-going and new projects for 2011.
- Review and discussion of the Mission mid-channel/Qualark DIDSON project.

April 14th, 2011

- Fund performance and Q4 2010 review.
- Alternative asset classes update and discussion.
- Habitat Restoration Technical Committee Co-Chairs Presentation.
- Outlook for 2012. Potential for a call for Proposals.

September 15th, 2011

- First round selection of project concepts to be invited to proceed to stage two.
- On-going project status and review.

December 13th, 2011

- Analysis of third party proposal review processes.
- Second round selection of detailed proposals for funding in 2012.

Investment Sub-Committee Meetings

An Investment Sub-Committee of the Joint Northern and Southern Fund Committees met twice during 2011. Members were David Bedford, Frank Quinn (June only), Larry Peck and Don Radford.

June 1st, 2011

- Real estate manager search and interview process.
- Managers interviewed were Invesco (selected), Prudential and UBS.

December 2nd, 2011

- Listed infrastructure manager search and interview process.
- Managers interviewed were Brookfield, Lazard and RARE (selected).

2011 Call for Proposals for projects in 2012/13

The value of the Northern and Southern Funds grew gradually through 2010 and the first four months of 2011 to April, as the economy recovered from the effects of the 2008/09 financial crisis and subsequent weak investment climate. These gains were eroded through the balance of the year in volatile market conditions, yet sufficient gains were made for both Funds to issue Calls for Proposals in mid-2011 for projects starting in 2012.

In April 2011 the Northern Fund Committee determined that up to \$3.2M US might be available in 2012 to fund on-going, multi-year project commitments and new projects in 2012. The Committee had 18 on-going projects requesting further grants totaling \$1.4M in 2012 and received a total of 87 proposals for new projects requesting \$7.5M US. At the first round review meeting in September, 34 of the new proposals were selected to move to the second round detailed proposal stage along with the on-going projects. Bilateral technical reviews of the detailed proposals took place in January 2012 and a final decision on 2012 funding will be made at a meeting of the Fund Committee in February 2012.

Also in April, 2011 the Southern Fund Committee forecast that up to approximately \$2.4M US might be available for its 7 on-going projects and for new projects in 2012. The Southern Fund received 93 project concepts requesting \$7.3M US. During the first round review process in mid-September the Southern Fund Committee short-listed 41 proposals to move to the second stage requesting \$3M US. Southern Fund independent third party technical reviews took place in early December 2011. The Committee met in December to consider the findings of the technical reviewers and to develop a draft list of approved proposals. Final project selection took place in January, 2012 with 20 new proposals being selected for funding along with the 7 on-going projects for a total amount of \$2.23M US.

Project Audit

The accounting firm KPMG was again hired in 2011 to undertake an audit of selected project financial records. KPMG was directed to examine 13 projects and to tie their financial

accounting back to the financial summaries provided with each project's final report. The projects chosen were a representative sample from the organizations that the Fund commonly grants funds to including DFO, ADFG, NWIFC, WDFW, NOAA, consultants and First Nations. Specified procedures were applied to the projects and two different techniques used to select invoice items for back-up checks depending on the type and size of the project. This work is still underway.

Committee Appointments

Dr. Denis D'Amours has been representing Canada in an "acting" capacity on the Northern Fund Committee since mid-2011, replacing Mr. Frank Quinn.

Yukon River Panel Restoration and Enhancement Fund

In March 2011 PSC Fund staff took over responsibility for the administration of the Yukon River Panel's Restoration and Enhancement Fund. Final decisions on the list of 2011 projects were made by the Panel in March and the first order of business for Fund staff was to issue contracts for 31 projects in the amount of \$1.14M US. The Call for Proposals for projects starting in 2012 was prepared using PSC standard formats and guidelines and was issued on schedule in August. First round project concepts were collected in early October and sent for review. The initial bilateral review process, which hitherto had taken a day and a half, took 2 hours and was ratified by the Panel's Joint Technical Committee in 15 minutes. Instructions to proponents approved to move to the second round were issued in December. A second round review is currently underway and final funding decisions will be made in March 2012.

The use of PSC standard contracts, application forms, budgets, reporting requirements, etc. undoubtedly resulted in more e-mail and phone traffic for Fund staff answering questions and guiding grant applicants and recipients. The additional work load on Fund staff was well within expected bounds and is anticipated to reduce over time as the new administrative procedures become familiar to Yukon proponents.