



**Annual Report of the
Southern Boundary Restoration and Enhancement Fund and the
Northern Boundary and Transboundary Rivers Restoration and Enhancement Fund
for the year 2004.**

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 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 manage the funds.

Committee Members

Northern Fund Committee

Canada:

John Lubar, Co-Chair
(David Einarson for John Lubar)
Gord Zealand
Ron Fowler

United States:

Jim Balsiger, Co-Chair
David Bedford
Jev Shelton

Southern Fund Committee

Canada:

Ron Kadowaki, Co-Chair
(E. Lochbaum/W. Luedke for Ron Kadowaki)
Don Hall
Bill Otway

United States:

Rollie Rousseau, Co-Chair
Larry Rutter
"JP" Olney Patt

Executive Summary

- Total contributed capital (nominal) at year end was \$CDN 209,796,000 or \$US 140,065,000. Actual fund asset value at December 31st was \$CDN 211,693,000 or \$US 175,874,000. The much greater growth in asset values when expressed in U.S. currency (\$US 35,809,000) as compared to Canadian currency (\$CDN 1,897,000) is due to the significant appreciation of the Canadian dollar relative to the U.S. dollar since the funds were capitalized.
- The rebound in equity markets in the latter part of 2003 continued in early 2004 but then slowed by June and struggled to make much headway for the balance of the year.
- The U.S. bond component of the Fund portfolio was switched to Canadian bonds in June to achieve a better balance of US and Canadian currencies.
- The Fund terminated its relationship with MFS, manager of its U.S. equity portfolio, primarily due to a pattern of underperformance since being engaged three years earlier, and other issues; the funds they managed were transferred to the Barclays Russell 3000AT Fund in December.
- Putnam, manager of the EAFE portion of the equity portfolio, was put on watch for much of the year due to underperformance and other issues. The decision was later made (January, 2005) to terminate the Fund's relationship with Putnam and to initiate a search for a value-oriented manager to replace them.
- The Southern Fund Committee supported a total of 41 projects for U.S. \$2 million or CAN \$2.6 million.
- The Northern Fund Committee supported a total of 22 projects for U.S. \$1.9 million or CAN \$2.4 million.
- Northern and Southern Fund Committee members met jointly four times in 2004. The Southern Fund Committee met eight more times on their own and the Northern Fund Committee six more times.
- On the Canadian section, David Einarson was appointed to the Northern Fund Committee, replacing John Lubar. Ron Kadowaki was temporarily replaced on the Southern Fund Committee, initially by Ed Lochbaum and latterly by Wilf Luedke.
- The Fund Coordinator finished a part-time secondment with the Pacific Salmon Foundation in Vancouver, B.C. in March, 2004.

Investment Review

Equity markets got off to a strong start in early 2004 and the contrast with the beginning of 2003 could not have been more marked. The Fund earned 4.7% in the first quarter exceeding the 4.1% benchmark result. Brandes turned in another solid global equity result. MFS also performed well. Putnam trailed the index for a fifth consecutive quarter.

In the second quarter the New Year enthusiasm began to evaporate. The Madrid bombings were partly behind the turn in sentiment together with concern about the stability of Middle East oil supplies. Cash outflows and currency losses impacted the Fund. Brandes performed well for another quarter; MFS slightly outperformed their index, but Putnam trailed for a sixth consecutive quarter.

By the third quarter, weaker than expected economic indicators in the U.S. such as industrial production, employment figures and consumer spending suggested that the economic recovery of the early months was failing to live up to expectations. The U.S. bond component was switched to Canadian bonds in June and in the third quarter bond gains were enough to offset losses in equities, particularly U.S. and Global equities.

While economists had expected a deceleration from the surge that marked the beginning of 2004, the environment had weakened by the fourth quarter more than most had anticipated and equity markets continued to struggle to make headway, held back by the nagging doubt that the slowdown may have further to run. This may well be the case in the euro zone and Japan, however in the U.S. the economic climate appears to have stabilized thanks in part to the fall in the U.S. dollar and the boost this gives to exporters.

Total contributed capital (nominal) at year end was \$CDN 209,796,000 or \$US 140,065,000. Actual fund asset value at December 31st was \$CDN 211,693,000 or \$US 175,874,000. The much greater growth in asset values when expressed in U.S. currency (\$US 35,809,000) as compared to Canadian currency (\$CDN 1,897,000) is due to the recent and very significant appreciation of the Canadian dollar relative to the U.S. dollar since the funds were capitalized.

Contributed capital and asset value of the individual Funds as of December 31, 2004 stood as follows:

	Contributed Capital		Asset Value	
Northern:	\$CDN 112,388,000	\$US 75,000,000	\$CDN 113,404,000	\$US 94,216,000
Southern:	\$CDN 97,408,000	\$US 65,000,000	\$CDN 98,289,000	\$US 81,658,000

Note: In 2003 a rescission of 0.65% reduced the 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

2004 Project Funding

In June 2004 the Northern and Southern Fund Committees were pleased to announce an inaugural round of 63 projects had been approved by the Committees for 2004/05 for a total expenditure of more than U.S. \$3.9 million or CAN \$ 5.1 million.

In selecting projects for this inaugural round of funding, the Northern and Southern Fund Committees requested the advice of the Pacific Salmon Commission's Panels and Technical Committees, recognizing that they were well placed to identify priority stocks and habitats; the information needs of the Parties; and, other requirements for implementation of the Pacific Salmon Treaty.

The Southern Fund Committee supported a total of 41 projects for U.S. \$2 million or CAN \$2.6 million. Proponents included Canadian and U.S. government agencies, First Nations, tribes, fishermen's associations, academic institutions and community groups from B.C. and Washington and Oregon States. These included:

- A project to use new sonar technology to improve the accuracy of in-season estimates of total salmon escapement in the Fraser River that will help managers develop and adjust in-season fisheries management plans based on more accurate data inputs.
- A feasibility assessment to determine if fishwheels, which have proven to be a successful assessment tool for coho salmon in the Fraser River, can be operated during the annual sockeye migration period when river flows peak.
- Support for the Nooksack Basin Stream Restoration Crew in Whatcom County, Washington, who will undertake a number of in-stream structural improvements to restore riparian habitat and function to salmon-bearing streams throughout the watershed.
- A habitat restoration project on the Deschutes River in Oregon by the Confederated Tribes of the Warm Springs Reservation. Deschutes River fall chinook salmon are used by the U.S. Chinook Technical Committee of the PSC as an indicator stock to assess the effectiveness of abundance based harvest management.

The Northern Fund Committee supported a total of 22 projects for U.S. \$1.9 million or CAN \$2.4 million. Proponents included 5 First Nations from northern B.C. and the Yukon; collaborative projects co-managed by Fisheries and Oceans Canada and the Alaska Department of Fish and Game and a range of other habitat restoration and fisheries management projects led by Fisheries and Oceans Canada. These included:

- A two-year joint Canada/U.S. project to develop and implement an effective, cost efficient Tuya River sockeye harvest system consistent with the Transboundary Annex provisions of the Pacific Salmon Treaty.

- A two-year study to provide in-depth information about the distribution and abundance of emigrating Tuya River sockeye salmon in the Stikine River and their spawning behaviour and level of success.
- Improved sockeye salmon stock identification techniques to better evaluate existing run reconstruction methods by providing accurate and timely estimates of stocks caught in Canadian and U.S. fisheries in the Northern Boundary area.
- A logging debris removal project on Oweekeno Lake which will restore critical lake shore habitat for spawning salmon and rearing fry, as part of a larger general recovery plan for salmon in Rivers Inlet on B.C.'s central coast.

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 at least for the time being. Thus the Joint Fund Committee met by telephone conference call once (January 6th, 2004) and in person on three occasions (May 27th and 28th, 2004; October 18th, 2004; and November 16th and 17th, 2004).

The Joint Committee's first meeting in 2004 was a conference call held on January 6th, 2004. John Myrah of Hewitt and Associates provided an assessment of his firms' understanding of the current situation at Putnam Investments. He reviewed the regulatory issues raised by the SEC investigation of Putnam and Putnam's reaction to the investigations findings. He discussed Putnam's performance over the short and long terms; their position relative to their peers and their investment style. He also took a number of questions from Committee members regarding the costs to the Fund of transferring out of Putnam as an investment manager. The Committee tasked Mr. Myrah with collecting further information on performance and transfer costs and agreed to ask Putnam to send its representatives to meet with the Joint Committee when they next met in May.

The second meeting of the year was an in person meeting held at the PSC offices in Vancouver on May 27th and 28th. John Myrah and Sean Macaulay of Hewitt and Associates in their capacity as consultants to the Fund Committee brought forward a re-examination of the Fund's US equity structure with a view to potential investment structure improvements and opportunities for diversification now that the Fund is fully invested and overall assets are larger. After hearing their briefing and discussing the pros and cons the Committee requested Hewitt to prepare a search document exploring opportunities offered by passive and enhanced-passive large cap and active small/mid cap US equity managers and to report back to the Committee in October. Also on the agenda was an in person meeting with representatives from MFS, the Funds US equity managers. Items that were discussed included a change in management fee structure in place of a long-expected transfer of the account to a pooled fund

vehicle which although initially offered by MFS had now been unexpectedly withdrawn as an option. There was also discussion about the firm's performance record as managers of the Fund's US equities portfolio and also a report on MFS's response to a recent SEC investigation and the changes implemented as a result. Representatives from Putnam were also invited to address the Committee in person. The Committee had requested this meeting to hear firsthand about the continuing fallout from the SEC investigation, the subsequent restructuring at Putnam and the effect these changes were having on the performance of the Fund's investments.

The third meeting of the year was an in person meeting held in Victoria, BC on October 18th, 2004. John Myrah of Hewitt and Associates opened the meeting by providing Committee members with an in-depth update on the recent performance of MFS and Putnam. Sean Macaulay of Hewitt and Associates then took the Committee back to the issue of US equity structure options last discussed in May. From these briefings the Committee took due note of the fact that over the past four years MFS's performance had not been satisfactory and the Committee had no confidence in MFS's assurance of a turnaround. Viable alternatives were available that would achieve a higher annual yield while protecting the principal of the Fund. Therefore a motion was passed to terminate the Funds relationship with MFS and move to an alternative US equity structure. Mr. Myrah was tasked with bringing forward a shortlist of potential replacement managers to MFS with whom the Fund Committee could invest their US equity portfolio.

The fourth and last Joint Fund Committee meeting of the year was an in person meeting held at the PSC offices in Vancouver, BC on November 16th and 17th, 2004. As usual the November meeting was marked by the annual Fund investment manager performance report and interviews. The Committee was generally satisfied with the performance and reports from Barclays Global Investors and from Brandes Investment Partners. The interview with Putnam Investments covered the company's on-going challenges since its investigation by U.S. mutual fund regulators. In particular, the Committee was very concerned about poor performance. The Putnam representatives offered a fee break; recommended staying the course and urged the Committee to trust in the improvements they'd made to their business. As they had done in October with MFS, Hewitt and Associates staff had prepared a four year performance evaluation of Putnam and a review of alternative strategic investment options for the Committee to consider now that the Fund was fully invested. There was a lengthy debate on Putnam's record and future prospects and on the pros and cons of diversifying the Funds investment style bias. The outcome was to task John Myrah with preparing an in-depth analysis of structural and style-related reasons for changing the Fund's non-North American equity manager and to bring forward a list of potential alternative managers. (Note: at a subsequent meeting in January 2005, the Joint Committee decided to replace Putnam with a value-biased investment fund to be managed by a new manager, and set in motion a process to select a candidate).

Southern Fund Committee Meetings

The Southern Fund Committee met eight times during 2004.

January 27th, 2004. Teleconference.

- Following the rapid recovery of the equity market, the Committee examined the potential for “jump starting” project funding in 2004.
- Placed Putnam Investments on a “watch list” footing.

February 9th, 2004

- Report from Hewitt and Associates on Putnam Investments.
- US \$2 million set as funding target for 2004 and “expression of interest” document to be prepared to solicit project proposals.

May 17th, 2004

- Project selection meeting for 2004.

May 28th, 2004

- Various outstanding particulars regarding 2004 projects.
- Consideration of early strategic issues in the preparation for 2005/06

June 3rd, 2004. Teleconference.

- Project detail discussion with the US and Canadian FRAM project leaders.

July 15th and 16th, 2004

- Update on 2004 projects and program administration.
- Strategic issues concerning the 2005/06 season.
- Details of the 2004 Call for Proposals, Technical Review, Evaluation Criteria and Timetable.

October 18th, 2004

- Proposal Review Team nominations and budget setting.

December 7th and 8th, 2004

- Initial project selection meeting for 2005/06.

Site visits

On three separate occasions, several members of the Southern Fund Committee visited some of the projects that had been funded for 2004. These site visits are considered to be an important aspect of the Committee’s ongoing oversight responsibilities. In August, two committee members and the Fund Coordinator visited the fishwheel project on the Fraser and several of the habitat restoration sites on the Thompson River in BC. In November a member of the Southern Fund Committee and the Fund Coordinator visited the Nooksack Stream Restoration

Team in Bellingham, Washington. And in December, another Committee member and the Fund Coordinator visited Cultus Lake to observe the underwater video camera equipped ROV in action in the field. The members felt that these visits were highly informative and would provide insights into the selection of future projects

Northern Fund Committee Meetings

The Northern Fund Committee met seven times during 2004.

February 13th, 2004. Teleconference.

- Report from Hewitt and Associates on Putnam Investments.
- US \$2 million set as possible funding target and a draft call for proposals document to be prepared to solicit project proposals.

April 5th, 2004. In person and teleconference.

- First round project review meeting for 2004.

April 16th, 2004. Teleconference.

- Final project selection meeting for 2004.

May 28th, 2004

- Consideration of early strategic issues in the preparation for 2005/06

August 4th, 2004. Teleconference.

- Details of the 2004 Call for Proposals, Technical Review, Evaluation Criteria and Timetable.

September 27th and 28th, 2004

- First round “Project Concept” review meeting and shortlist selection for 2005/06

November 18th, 2004

- Technical Review Team nominations, Evaluation Criteria and Timetable.
- Strategies for growing the “corpus” of the Fund to US \$100 million.

2005 Call for Proposals

During the summer of 2004 both the Northern and Southern Fund Committees reviewed the earnings from the Fund’s investments and found that according to their spending policies, a second round of project funding could be undertaken in 2005. The Southern Fund set a target budget figure of U.S. \$3.0 million and the Northern Fund U.S. \$2.9 million. The Fund Coordinator was tasked by the two Committees with drafting each of them a Call for Proposals package that would include a more sophisticated proposal announcement, technical review and project selection process.

The Southern Fund Committee refined the Application form used in 2004, developed a suite of evaluation criteria and a scoring methodology to accompany them. They also established two independent, bilateral proposal review teams to assist the Committee in project selection. They set out a timetable that called for the issuance of the Call for Proposals in late August, proposal

review by the independent teams in November, initial project selection by the Fund Committee in December and final project selection in January 2005. For 2005, the Committee sought to strike a better balance between information gathering projects, which dominated the set of projects funded for 2004, and habitat and enhancement projects. As a result, approximately half the funding for 2005 projects was expected to go towards habitat and enhancement type projects.

The Northern Fund Committee adopted a two-stage approach requiring applicants to submit a brief 2 page project summary for initial review by the Committee themselves. This yielded a shortlist of proponents who then completed a version of the improved Application Form developed for the Southern Fund Committee. The short-listed proposals were forwarded to a team of Alaskan and Northern BC and Yukon expert reviewers in December. The reviewers met in person in January and final decisions are expected to be made by the Northern Fund Committee in early March 2005.

Committee Appointments

Mr. David Einarson was appointed to the Northern Fund Committee in the capacity of Canadian co-chair and Northern Panel representative in October 2004, replacing Mr. John Lubar. Mr. Ron Kadowaki was temporarily replaced on the Southern Fund Committee, initially by Mr. Ed Lochbaum and latterly by Mr. Wilf Luedke, while Mr. Kadowaki completes a special assignment.

Fund Coordinator

Mr. Angus Mackay the Fund Coordinator completed a second consecutive 6-month part-time secondment with the Pacific Salmon Foundation in March 2004. The secondment was a cost saving measure and an opportunity for professional development, undertaken at a time when the Fund was gradually re-building following a down-turn in global economic markets and no funds were available to support projects.