Legislative Assembly of Alberta

The 27th Legislature
Third Session

# Standing Committee
# on the
# Alberta Heritage Savings Trust Fund

Wednesday, December 15, 2010
11 a.m.

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**Legislative Assembly of Alberta**
**The 27th Legislature**
**Third Session**

**Standing Committee on the**
**Alberta Heritage Savings Trust Fund**

Tarchuk, Janis, Banff-Cochrane (PC), Chair
Elniski, Doug, Edmonton-Calder (PC), Deputy Chair

Blakeman, Laurie, Edmonton-Centre (AL)
DeLong, Alana, Calgary-Bow (PC)
Forsyth, Heather, Calgary-Fish Creek (WA)
Groeneveld, George, Highwood (PC)
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Quest, Dave, Strathcona (PC)

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| Aaron Brown | Director, Portfolio Management |
| Nick Kaczmarek | Public Affairs Officer |
| Rod Matheson | Assistant Deputy Minister, Treasury and Risk Management |

**Alberta Investment Management Corporation Participants**

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| Leo de Bever | Chief Executive Officer and Chief Investment Officer |
| Pine Pienaar | Senior Vice-president, Client Relations |

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**11 a.m.** **Wednesday, December 15, 2010**

[Ms Tarchuk in the chair]

**The Chair:** Well, good morning, everyone. I'd like to call this meeting to order and welcome everyone. I'm Janis Tarchuk, MLA for Banff-Cochrane. I wonder if I could just go around the table and ask committee members and all of our attendees to introduce themselves for the record, and we'll start with Doug.

**Mr. Elniski:** Yes. Good morning. Doug Elniski, MLA, Edmonton-Calder.

**Mr. Groeneveld:** Good morning. George Groeneveld, MLA, Highwood.

**Mr. Johnston:** Good morning. Art Johnston, Calgary-Hays.

**Mr. Kaczmarek:** Nick Kaczmarek, Alberta Finance and Enterprise.

**Mr. Pienaar:** Pine Pienaar, AIMCo.

**Dr. de Bever:** Leo de Bever, AIMCo.

**Mr. Matheson:** Rod Matheson with Alberta Finance and Enterprise.

**Mr. Brown:** Aaron Brown, Alberta Finance and Enterprise.

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**Ms LaFave:** Betty LaFave, office of the Auditor General.

**Mr. Saher:** Merwan Saher, Auditor General.

**Ms Sales:** Tracey Sales, communications services with the Legislative Assembly Office.

**Mr. MacDonald:** Hugh MacDonald, Edmonton-Gold Bar. Good morning.

**Mr. Quest:** Good morning. Dave Quest, Strathcona.

**The Chair:** Okay. Thank you.

Heather, you're with us on the phone?

**Mrs. Forsyth:** Hi, Chair. Good morning, everybody. Greetings from Calgary. Merry Christmas.

Chair, I have to apologize. I'm going to have to sign off in 15 minutes. I have a sick mum, that I have to get to the doctor.

**The Chair:** Okay. Well, all the best with her.

**Mrs. Forsyth:** Thank you.

**The Chair:** So everyone has a copy of the agenda. I wonder if someone could move that the agenda for December 15, 2010, of the standing committee is adopted. Art. All those in favour? No objections? That motion is carried.

In your package you've got minutes of the September 28 meeting. Would someone like to move those as circulated?

**Mrs. Forsyth:** I'll move that, Chair.

**The Chair:** Okay. Thank you, Heather. All those in favour? That motion is carried.

The Alberta heritage savings trust fund's second-quarter update was distributed to all members on November 30, 2010. As you know, our act indicates that one of the functions of the committee is "to receive and review quarterly reports on the operation and results of the operation of the Heritage Fund."

I'm pleased that Rod Matheson, assistant deputy minister, treasury and risk management, Alberta Finance and Enterprise, is here with us. Rod, I wonder if I could just pass it over to you for a few comments.

**Mr. Matheson:** Certainly. I'd be happy to.

Madam Chair, good morning. Minister Morton is unable to attend this morning, so in his absence I'm pleased to provide you and the committee with a brief review of the second-quarter update for the heritage fund. In a nutshell the second quarter saw improved overall performance for the fund. The heritage fund's value is up over the last fiscal year, and gains made in the second quarter have more than offset the losses seen at the end of the first quarter. Positive returns in world equity markets helped the fund make net gains of $391 million in the second quarter, offsetting the first-quarter loss of $164 million. This brings total net income for the heritage fund in the first half of fiscal 2010-11 to $227 million.

The fund's fair value at September 30, 2010, was $14.8 billion, which is a $444 million increase from March 31, 2010. This is made up of the $227 million in net income that has been realized as well as an increase in unrealized gains. Unrealized gains represent profit that would be made if assets were sold at current prices.

Just briefly looking at investment performance, on a fair value basis the fund's investments gained 5.7 per cent in the second quarter. Again, that offsets a first-quarter loss of 2.1 per cent. This brings the total return for six months to 3.4 per cent, with virtually all asset classes posting gains for the six months ended September 30, 2010. Canadian equities, which are about 12 per cent of the total fund, have returned 4 per cent over the first six months of the fiscal year. Fixed income, or bonds, which is about a quarter of the total fund, has returned 6.5 per cent, and real estate, which is about 12 per cent of the fund, earned 7.2 per cent in the first half of the year.

Looking ahead, the heritage fund is now forecast to earn investment income of $741 million after expenses for fiscal 2010-11. As per the legislation income generated by the fund less the amount retained for inflation-proofing is transferred to the general revenue fund to support government programs. Based on current forecasts, the amount that will be retained for inflation-proofing is $304 million.

That concludes my brief review of the second-quarter report, and we'd be happy to answer any questions by the committee.

**The Chair:** Are there any questions? Hugh.

**Mr. MacDonald:** Yes. The first question I have. I have a number this morning. On page 4 of the second-quarter update the second paragraph states: "According to the Fund's business plan for the fiscal year 2010-11, the Fund was expected to earn net income of $976 million, after expenses of $74 million, and retain $291 million in the Fund for inflation proofing." Now, the second-quarter update had an anticipated amount of investment income of slightly more than that, $1,050,000,000. It is indicated there that there would be $235 million set aside for inflation-proofing, and the forecast there is for income of $815 million. Can you explain the reason, please, why the numbers from the second-quarter update are different than the numbers that you have on page 4?

**Mr. Matheson:** I'm sorry. I'm not sure of the numbers you're referring to.

**Mr. MacDonald:** I'm referring to the numbers in the second-quarter update and the numbers on page 4, the second paragraph, of your second-quarter review.

**Mr. Matheson:** Unfortunately, I did not bring a copy of the government's second-quarter report. May I ask: is that heritage fund?

**Mr. MacDonald:** Yes.

**Mr. Matheson:** Yes. Sorry. The answer to the question is that when we report numbers in the government's budget figures, these would be gross. These would be before expenses. Our investment income forecast for the heritage fund before expenses is $815 million. What we report in the second-quarter report for the heritage fund is $741 million after expenses. So the only difference between the two numbers is the expenses.

**Mr. MacDonald:** And the expenses have changed?

**Mr. Matheson:** Yeah. The expense is also a forecast, so it would also change from quarter to quarter.

**Mr. MacDonald:** Okay. I guess that answers that question.
Can I get back on the list, please?

**The Chair:** Okay.
Actually, I'd just like to note for the record that Alana DeLong from Calgary-Bow has joined us.
Doug.

**Mr. Elniski:** Good. Thank you. Good morning, gentlemen. It's good to see you here on such a lovely, lovely Alberta day. I note with some interest that the only real nonperforming asset that we're dealing with here in terms of the asset categories today is actually timberlands, which is kind of interesting considering that for the first time in about the last four years we've actually seen some positive gains on the commodity side of lumber. I'm just kind of curious if there's some correlation there, or what's going on on that one?

**Dr. de Bever:** There isn't really a correlation between lumber prices and timberland, at least in the short run. In fact, a lot of the uses of timberland aren't in lumber. There's another issue in that the valuation of timber assets tends to be infrequent, so the short-term correlation can be quite spurious, frankly. We still think that long term, timberlands are a good investment, and we're making some more. That will probably be announced within the next couple of months. The reason we like them is that in the long haul timber is the only commodity that sort of holds its real value over time. It rises with inflation. So those characteristics tend to be good for both the heritage fund and for the pension plans that invest in this asset class.

**Mr. Elniski:** Wonderful. Thank you.

**The Chair:** Alana and then Dave.

**Ms DeLong:** Thank you. I've got a couple of questions, but first of all the question I asked last time I want to ask again, and that is: are you getting enough flexibility in terms of the directions that you are receiving from the finance department in order to manage the funds to the most benefit of Albertans?

***11:10***

**Dr. de Bever:** There is no direct participation of finance in anything we do on a day-to-day basis. The communication we have with finance is through the investment plan, the asset mix, and beyond that, really, there is no direction. We have discussions with finance on the appropriateness of, say, being invested in private equity or fixed income versus equities. That's the extent of the communication, and frankly that part of the relationship has worked very, very well both from a political and an administrative point of view.

**Ms DeLong:** Thank you.

**The Chair:** Dave.

**Mr. Quest:** Thank you. Just on page 5, looking at our second-best performing asset, it has been real estate appreciation. My understanding is that our holdings are virtually all commercial. Correct me if I'm wrong there. This 7.2 per cent increase: are these existing holdings principally that we had that were reduced in value during the recession and just reflect the current-day value, or did we purchase a lot of real estate when it was softer last year?

**Dr. de Bever:** It was probably a combination of both. You may have seen reference to the ING transaction in the press that we completed recently in industrial properties. But, again, it is very, very difficult on a six-month basis, which is what this table does, to say anything sensible about these things. Most of these investments in unlisted assets are made on a long-horizon basis, so it's very hard to interpret. For instance, the 4.7: I'm not even sure whether that has all the revaluations of the index, which is what that 4.7 is supposed to represent. The 7.2: there's probably some recovery out of the recession and some shift in capital market discount rates. To the extent that they go down, the value of the real estate goes up. Generally speaking, these things, the valuation of the real estate, are done by external evaluators, and they tend to lag reality by six months, nine months.

**Mr. Quest:** Okay. I want to do a supplementary if I may. Are all of our real estate holdings in Canada?

**Dr. de Bever:** No. We have some in the U.S., and we have some in the U.K. In fact, the U.K., because of the disorientation of the market down there, is presenting a lot of opportunity for us because we have the cash to deploy, and a lot of U.S. funds are hamstrung because they got themselves into trouble in 2007 and 2008 and don't have the liquidity we do.

**Mr. Quest:** Thank you.

**Mr. MacDonald:** Thank you, Madam Chair. My next question is from page 19 of the second-quarter report, Mr. Matheson. It's the investment expenses. It is noted, in note 8 actually, that "some investments are managed by third party investment managers selected and monitored by AIMCo." We know that they don't have the track record, their expenses are higher, and they have a dismal return. The assets shrank in value by $542 million last year according to AIMCo's annual report, page 26. Who are these third-party investment managers? How are they selected? Is it a competitive process? Who selected them, and for how long will they still maintain these contracts or options?

**Mr. Matheson:** Well, I'm going to turn it over to Leo just because all of the management of the fund, including the selection of who to use as external managers, is something that is entirely in the purview of AIMCo as our investment manager.

**Mr. MacDonald:** Well, sir, with all respect, in his annual report they refer to these contracts that they inherited. I will dig that up for you if you'd like. I would like you to answer, please, because according to them, they inherited this. If you look at page 17 of AIMCo's annual report, I'm going to quote directly. "AIMCo inherited a large number of external equity managers with relatively small and high-cost mandates." I think an explanation is in order. The deputy minister or the minister signs off on all this. They report to you, and I would appreciate an answer.

**Mr. Matheson:** When it refers to inheriting – I mean, I don't want to put words in AIMCo's mouth. I'll certainly ask Leo to supplement. I think the reference there is that pre becoming a corporation, they were AIM, Alberta investment management. They were largely at that time the same group of people that were employees of the finance department that were then moved into a corporation. The corporation inherited those external managers. The choice of those external managers was still made by the organization.

But I'd certainly let Leo supplement that.

**Dr. de Bever:** Well, I think the quote in our annual report is correct in that the philosophy – and I should point out right from the beginning that the group of people that were managing the funds at the time was relatively underresourced. The number of managers that they hired is not what I would have put in place. What we've done since – and that's probably more productive to speak about – is consolidate the roster of managers from 85 in the case of equities to about 15. The ones we retained should have the right criteria to produce value-added for us. I think 2009 was a particularly egregious year in that the contrast between, you know, the 70 guys that lost us money, effectively, and the internal staff was very, very wide. You don't expect that to happen every year.

We're not trying to say that external managers lose money and internal managers always make money. It's not always going to be the case. The point is that 85 managers was too much. The basis on which these mandates were let was probably not the brightest. If you give people more concentrated mandates, you get better terms, and that's what we've been doing in the last two years to make sure that the managers we do hire have a reasonable chance of outperforming the benchmarks that we've set for them and make sure that the government, or AIMCo, gets the best financial terms for having them manage the money.

Of course, the other thing we've done is, to the extent possible, where we can attract talent internally, take an external mandate and manage the money internally. You should understand that the cost differential is quite significant. It's about 3 to 1, sometimes more. In other words, I can do for a quarter or a third of the cost what is done externally. When you think about it, there's no magic to that. When you farm money out to an external manager, he has to cover his marketing expenses and the capital involved in the firm and all of that. All we pay for is the cost of the asset management.

Part of what we've done in the last two years is try and give the government better value for money. Dwelling on what went on in the past is probably not terribly productive, but we hope that we can show over the next two years that what we've done to improve the discipline around hiring managers and managing them will have a positive impact on the overall cost structure.

Speaking about cost structure, you should understand that a large part of the increase in the costs over the last few years has nothing to do with who were selected for managers. It's the complexity of the asset mix that the funds manage. In other words, about 10 years ago the asset mix that, say, a heritage fund or the pension plans held could be managed for .1, .15 per cent per year. But because of the diversification of the asset mix into real estate, mortgages, private equity – private equity in particular – and externally managed listed equity, that cost has almost, well, tripled, more than tripled. There's nothing wrong with that in principle as long as you understand that that's the driver behind the cost. In other words, as long as the cost has a payoff, then it can be justified from the standpoint of giving value for money. So on its own a cost number isn't terribly important, even for an external manager. If an external manager gives me 2 per cent and I have to pay him .4 per cent to earn that 2 per cent, that's a good value. It's just that we'd like to have the odds of getting that kind of ratio improved relative to what it was.

***11:20***

**The Chair:** Okay. Before I move to Alana, I just want to welcome Laurie Blakeman, MLA for Edmonton-Centre, and I know that she'll want to welcome us to her constituency.

**Ms Blakeman:** Thank you. Some days my constituency isn't quite as fabulous as it is other days. It's kind of hard slogging today. Nonetheless, it's very Christmas-like, and we are getting closer to Christmas, so it's still the fabulous constituency of Edmonton-Centre.

**The Chair:** Okay. Alana.

**Ms DeLong:** Thanks very much, Janis. One of the other hats I wear is government liaison for Alberta Innovates: Health Solutions, so I'm really aware of the need for money in angel funds, money being invested in Alberta. But at the same time I remember how we got really slapped down by one of your early decisions where you invested in an Alberta company, Precision Drilling. Is there any way that you see that your organization could somehow be involved with angel funds for specifically Alberta without getting us into political hot water?

**Dr. de Bever:** I get two criticisms, that I invest too much in Alberta and that I invest too little in Alberta. There is an additional problem. I introduced venture capital to Ontario Teachers' when I was there, and that's really what your angel funds fit into. It's the toughest asset class to manage as a pension plan because it's incredibly labour intensive, and the odds of making money are pretty low. If you make 10 investments, chances are that three or four are going to go bust in the first year, three or four are going to be okay, and if you're going to make any money, it will be off the one or two that are left. So it's a very challenging asset category. I have been involved with various groups operating here that are trying to get more money available for angel funds and for venture capital, and I haven't found the magic button to do it.

What's the outlook? I mean, we're trying to find a way to be helpful, but at the same time we have to do it not to be nice to the province; we have to do it on commercial terms. That is our mandate. If we can do it on those terms, we will make every effort.

Further to the question underneath your question – and that is, "Is it more difficult to do this in Alberta than elsewhere?" – the answer is yes. We always apply a second screen along the lines of: "Okay. It's a good idea. Now, is the population of Alberta going to perceive it as a good idea?" Sometimes you run up against obstacles where you say, "Well, we're probably not the best vehicle to do this," but at the same time we feel that if it is a good idea and we can take the flak for doing it, we will. Or I will. But it's very difficult because we have to have the resources in place to manage those kinds of investments, and that's the tough part.

**Ms DeLong:** Thank you.

**The Chair:** Hugh.

**Mr. MacDonald:** Yes. Thank you. I am not satisfied with the answers I received to my last question.

**Dr. de Bever:** Didn't you get an answer to that?

**Mr. MacDonald:** Who are these external managers?

**Dr. de Bever:** Who are they? Well, I mean, there are hundreds of external managers out there. The selection process probably was: what is their most recent performance over a four-year period? Based on that, they probably made presentations that they were in a good position to make money for the heritage fund or for Alberta in general. Unfortunately, as you probably always see in the fine print in the newspaper, past performance is not indicative of future performance, and a number of these things did not perform going forward they way they did historically. Who are they? Well, they're the who's who of what's out there. How specific do you want me to be on that?

**Mr. MacDonald:** Well, this is more to Mr. Matheson, Madam Chair. I'm of the impression that these contracts were signed prior to the creation of the Crown corporation AIMCo. Now, how would you write a contract where you have a loss of $542 million, yet there is a performance fee paid of $25.7 million? Someone has to take responsibility for that. Someone has to be accountable. How can you have such a loss yet pay out as a performance fee $25 million?

**Dr. de Bever:** It's not a performance fee. This is the difference. What we hold our internal managers accountable to . . .

**Mr. MacDonald:** These are external managers.

**Dr. de Bever:** Yeah. Okay. But let me make the contrast because it's important. When we pay bonuses internally, it is mostly based on financial criteria. In other words, if we make money for you as the heritage fund, a small slice of that, 5 cents on the dollar, ends up in bonuses being paid to managers. A lot of these external contracts are flat-fee contracts. In other words, you pay 30, 40, 50, or sometimes even 100 basis points of the assets, so .3 to 1 per cent of the assets, to the external manager independent of any performance. That's the way these contracts typically work.

If at the end of the day these managers didn't make any money, that's just too bad for the client. That's the way it works. Now, we have the option to fire them, and of course we did fire 70 of them, but that's the only recourse you have. The way these contracts are structured is that if you are happy with the past record or you can get your mind around hiring these people, you sign a contract that says that the manager gets .3 or whatever per cent per year of the assets independent of performance whereas internal . . .

**Mr. MacDonald:** If I could be excused, please, are those fees that you're talking about included in other investment costs, or are they included in this performance fee, or this bonus? There's quite a difference.

**Dr. de Bever:** No. In the annual report there are two lines. There's a base fee, and then there's a performance-based fee, right? The base fee is the .3 or .4 that I was talking about.

**Mr. MacDonald:** Okay. That's included in other investment costs, which for this external group would be an additional $126 million.

**Dr. de Bever:** Right.

**Mr. MacDonald:** They're getting well looked after for a very, very poor performance.

**Dr. de Bever:** Well, it used to be $180 million when I came in. It's now $126 million, so give me a break. These contracts cannot be changed quickly.

**Mr. MacDonald:** I thought you said you could fire them.

**Dr. de Bever:** In some cases you can, and in most cases we have. In 70 cases we have. In other cases you don't want to because the decisions were not all bad, or they were not all bad with the benefit of hindsight. If you have good managers that perform in an area where you cannot attract internal expertise, you would not be very bright if you didn't retain them, so we have retained some of those managers, but we did get rid of 70. It sometimes takes three months. Sometimes it takes a year, sometimes two years to terminate a contract depending on how it was written.

For instance, in the case of hedge fund managers it often takes one or two years because they have a clause in the contract that says that because of the nature of the investments that they have in place, they want to be able to hold on to your money with the proviso that if you want to pull it back, they get one or two years to pull the money out of whatever investment that they've put you into.

That's the difference. In some cases, like if it's a straight listed equity mandate, three to six months is usually all you need to get the money back, but in the more esoteric categories like hedge funds it can take a lot longer. In the case of private equity you're basically stuck for seven to 10 years. Unfortunately, a number of investments were made in 2006, 2007, and 2008 in that area that I will basically have to deal with for the next six years.

**The Chair:** Alana.

**Ms DeLong:** Well, thank you very much. When it comes to your fixed income, that includes mortgages?

**Dr. de Bever:** Yes.

**Ms DeLong:** Okay. Are those just Canadian mortgages?

**Dr. de Bever:** I think there are a few external mortgages, but most of them are Canadian, and most of them are very high grade and CMHC insured, which adds a level of security that you wouldn't have with any mortgage.

***11:30***

**Ms DeLong:** Okay. What else would you include in fixed income?

**Dr. de Bever:** Fixed income is basically government bonds, nominal and real. Real would be a real return bond, which is linked to inflation, and it would be credit, meaning corporate bonds. Well, that's basically it, right?

**Ms DeLong:** And the mortgages?

**Dr. de Bever:** And the mortgages.

**Ms DeLong:** Okay. Thank you.

**The Chair:** Hugh.

**Mr. MacDonald:** Yes. My next question would be: what is the total of the $14.8 billion in heritage savings trust fund assets that are managed externally?

**Dr. de Bever:** It's about 20 per cent. It mirrors what goes on in the pension plans, but it's somewhere in that neighbourhood, right?

**Mr. Matheson:** Yeah. I don't think it's contained in this report.

**Dr. de Bever:** Overall, that's what it is. It might be a bit higher for the heritage fund because its stance is a bit more aggressive than some of the other ones, which is fine because this is an endowment. The difference between endowments and pension plans is that the pension plans are supposed to be long-term investors, but they have a three-year valuation cycle, so they have to be a little bit more – did you find the number?

**Mr. Matheson:** We can put that information together, and through the chair we can provide it to the committee.

**Mr. MacDonald:** I appreciate that.

Now, I have another question if you don't mind. In 2009-10 you had $71 million of annual investment expenses, and that does not include external management performance-based fees, as I understand it. Is that $71 million obviously included in the $229 million that's in your report? That's correct?

**Dr. de Bever:** It is, yes.

**Mr. MacDonald:** Okay. That's 30 per cent of $229 million. Why are the fees, these investment expenses, so much higher in the Alberta heritage savings trust fund than they are in LAPP or the general revenue fund or any of the other pension funds or the sustainability fund, that you look after?

**Dr. de Bever:** Okay. The cost of managing an asset base – well, first of all, let me explain to you the cost at which we manage these assets. There's a survey called the cost-effectiveness management survey. It basically says that because of our size and because of our ability to manage internally, the overall costs on an apples-for-apples basis are low relative to anything else.

Now, your question is a little different: why are these costs higher than they are for . . .

**Mr. MacDonald:** The rest of the pool?

**Dr. de Bever:** Right. Now, there are two answers to that. The first one is that what we manage for the sustainability fund is something really straightforward. It's short-term bonds. The cost of managing short-term bonds: first of all, it's a hundred per cent internal, and it's very, very cheap; you know, .1, .2 per cent, something in that neighbourhood. Now, the pension plans don't all have the same asset mix, so the cost of managing that depends very much on how much they have in the highest cost assets of private equity and hedge funds.

To the extent that their asset mix varies, their costs will vary as well, and that's the main driver, really. If they all were in the same asset mix, their average cost would be, for the pension funds and endowments, somewhere in the neighbourhood of about 40 to 45 basis points, or .4 or .45 per cent. The overall cost of managing the $70 billion is in the high 30s, or .3 something per cent, and the reason for that, of course, is that the sustainability fund drags the average down because it's so cheap to manage.

Does that answer your question?

**Mr. MacDonald:** So if these external management performance fees are outside the $71 million, how much are they in total for the year 2009-2010?

**Dr. de Bever:** I think it was in our annual report. First of all, if I have to pay performance fees, that's a good thing because that means they actually made money.

**Mr. MacDonald:** Well, you've got to make money before I'm going to pay it.

**Dr. de Bever:** That's right.

The other ones bother me a lot more; I mean, if I have to pay people even if they didn't perform.

That's just the way of the world. I mean, most of our people don't get paid unless there is incremental return.

**Mr. MacDonald:** They're apt to get very wild at you because they provided $2.1 billion in increase, and they got $9 million in performance fees, and the guys that lost $542 million got $25 million. I'm sure they're going to bring that up at the staff meeting.

**Dr. de Bever:** I'm glad you're so supportive of my attempt to bring talent inside.

Yeah, it is a disconnect. But here's what you should understand. If you understand the dynamic, then you should understand my challenge. Yes, I'm bringing down the cost of doing this, but I'm still bringing people inside the organization that get paid a fair bit of money. In other words, talent costs money. You should understand that to the extent that this policy is successful, that will be its end result. We will have brought down costs significantly over what they were before. But the internal costs: I mean, they're not low. I can't go out and hire people at $50,000 or $75,000 to do these jobs.

I think that if the object of AIMCo is to be fruitful in the long run, it will be that you get the assets managed for a lower cost than we did before, probably .1 per cent lower than what I started with, and that the returns will be a per cent or so higher in the long run than they were before. Will that be every year? I've told you this before, that markets go up and markets go down. My guess at what markets are going to do is not going to be as good and my people's guess is not going to be as good every quarter or every year, but in the long run that's what you would expect. We will end up with about as low a cost structure as you can get for the complexity of what we've been asked to manage.

You should understand that that complexity is still increasing. In other words, the proportion of assets that fits into the high-cost category as dictated by our clients, the heritage fund and the pension plans, is still increasing. I don't have an issue with that as long as you understand that the more labour-intensive asset classes cost more money, whether it's internal or external. To the extent I can do it internally, I can obviously do it a lot cheaper, but I can't do it for free.

**Mr. MacDonald:** So risk management is different for different classes of investments, right?

**Dr. de Bever:** Yes. We have a risk system that does two things. It calculates the absolute risk in the assets and the relative risk, meaning the risk that is imposed by the active management of the assets. We control both very carefully because ultimately that's my scarce resource. My ability to earn a higher return is limited, well, first of all by the markets and what they'll give me, but it's also limited by the fact that there is a limited risk tolerance in the heritage fund and in the pension plans and even within the government's sustainability fund. It's that risk that I manage. In other words, I try to get the biggest return for that risk.

**The Chair:** Okay. I don't have any other questions. Doug?

**Mr. Elniski:** No. I don't have one.

**Mr. MacDonald:** I have another question, please.

**The Chair:** Okay.

**Mr. MacDonald:** It's in regard to AIMCo. AIMCo was mentioned in the Auditor General's report from October 2010. The Auditor General had warned that "without effective change management procedures, AIMCo may not be able to rely on [its IT systems to] provide complete and accurate information." As a member of this committee with oversight of the Alberta heritage savings trust fund the reliability of information is vital. Can you please tell this committee what you have done to follow up on the Auditor's recommendation in that time frame?

**Dr. de Bever:** Well, first of all, we completely agree with the assessment by the Auditor General. The Auditor General can speak for himself, but I would like nothing more than that all our systems would be up to date. Again, we have right now about eight to 10 fairly major IT projects on the go to bring us in line with best practice in the industry.

I think the concern that the Auditor has around change management is: how do you manage that process, and how do you make sure that in the midst of all that change you're doing the right thing and that you have the right controls in place? We are working very hard with the Auditor General's office to make sure that the way we're doing this is in line with what they expect us to do. It's going to take us another year or two, but at the end of that we will have as good a set of IT systems and control systems as any organization in the country.

***11:40***

**Mr. MacDonald:** Thanks.

**Mr. Saher:** I have nothing to supplement. I agree with Dr. de Bever's assessment. The most important thing for our office is acceptance that there is a challenge to put in a first-class IT internal control framework. We believe the organization accepts that, and that is the key to the change. I believe that the rate at which AIMCo plans to reinforce these systems, make them the best that they can be, is appropriate.

**The Chair:** Great. Thank you.

I wonder if someone would move that

we receive the second-quarter report as presented.

**Mr. Elniski:** I would certainly be happy to do that.

**The Chair:** Okay, Doug. All those in favour? Any objections? That motion is carried.

The fifth item on our agenda is the draft 2011-2014 business plan, which has been posted on the internal website. I wonder if at this point I could just maybe pass this over to you, Rod, to make a few comments on the business plan.

**Mr. Matheson:** Certainly. Again, I'd be happy to do that.

A general comment to start. This document has a slightly revised format and is significantly shorter than the business plan for the heritage fund from past years, and that's in keeping with the new approach that's being followed for all government business plans. This business plan has been approved by Treasury Board as required under the legislation, under the heritage fund act. As the act requires, it's now being brought to this committee for approval.

The heritage fund business plan outlines two goals. Goal 1 is to maximize long-term returns at a prudent level of risk. That's the primary goal of the heritage fund, and it speaks, really, to the fund's mission to provide prudent stewardship of the savings from Alberta's nonrenewable resources by providing the greatest financial returns on those savings for current and future generations as outlined right in the heritage fund act. The plan outlines two priority initiatives related to this goal and provides the key performance measures for the fund.

Goal 2, to ensure the heritage fund aligns with the fiscal goals of the province, speaks to the fact that it's important to view the heritage fund not as a stand-alone investment fund but, rather, in the broader context of the province's balance sheet. This includes, for instance, the ongoing work by the Department of Finance and Enterprise to evaluate the currency exposure of the heritage fund within the context of the province's broader fiscal landscape, including the U.S. dollar denominated resource revenues that we have.

Finally, I'll just point out that a third goal that was in previous business plans has been removed. This goal related to delivering information on the heritage fund to Albertans in a timely fashion. We believe that this goal was redundant to what is already required in the heritage fund act, and in the interests of brevity, under the government's new business plan format, the goal was removed. I will point out that the public reporting requirements are summarized in the introduction of the business plan, and we will continue to update Albertans regarding the heritage fund, as we have done in the past.

That concludes my brief comments. I'd be happy to answer questions.

**The Chair:** Hugh.

**Mr. MacDonald:** Yes. I read where the business plan explains in general terms the role of the Minister of Finance and Enterprise in relation to the heritage savings trust fund. In light of all the discussion recently and Ms DeLong's question – and the answer was quite interesting – about the relations between the ministry and the arm's-length entities, could you explain a little what role the minister of finance plays in the decision-making of AIMCo?

Now, I know it's defined in the Alberta Heritage Savings Trust Fund Act, and it has been noted in the past by yourself, I believe, at the last meeting of the committee that the minister of finance sets the asset mix. The oversight by finance is also mentioned several times in the latest report, and that goes back to Ms DeLong's question. The AIMCo vice-president, Mr. Gibson, at the last meeting said: "We work a lot with Rod" – with no disrespect – "and his staff to understand the needs of the fund so that we can where it makes sense skew things in the right way. We don't have any handcuffs, really, given the mandate and given the relationship with the finance staff." That was what was said, Madam Chair, but what is the actual working relationship?

**Mr. Matheson:** Well, as you've already alluded to, the minister ultimately is responsible for the way the heritage fund is invested, and that is carried out by the minister, with the staff of the ministry supporting him, working with the investment manager to develop the broad parameters which are contained in the asset mix that you spoke of as well as a key document, statement of investment policies, that is developed and then provided to AIMCo, and that really becomes the framework under which AIMCo then manages the assets. Within that broad framework and that broad asset mix the investment manager is then given the opportunity to invest the money to maximize returns.

On an ongoing basis once that's done, we do have a very good relationship at the working levels. Just like I think AIMCo would with the pension boards and their other clients, we meet on a regular, quarterly basis, and they provide us with an update on new developments, on performance, various asset classes, and how the performance is by asset class. We receive reports, and then we sit down and meet with them. I mean, at the working level that would be the relationship.

**Mr. MacDonald:** When the minister of finance or the ministry or the department sets the asset mix, does this then go for approval from Treasury Board?

**Mr. Matheson:** It's not required. The minister is responsible for the investments, so the minister sets the asset mix. He may choose to take it to his colleagues at, for example, Treasury Board for information, but it's not required by legislation.

**Mr. MacDonald:** Okay. Thanks.

**The Chair:** Any other questions?
Seeing none, I wonder if someone would like to move that we approve the 2011-14 business plan as circulated. Dave?

**Mr. Quest:** Sure.

**The Chair:** All those in favour? Any objections? That motion is carried.
At this point I'd like to thank the assistant deputy minister and his staff and just advise that we have some other business to go into. You're free to leave. Thank you very much. Safe travels to everyone, and Merry Christmas.

**Dr. de Bever:** The same to you.

**The Chair:** Okay. Our next item is that Tracey is going to give us an update on the Lethbridge public meeting. Tracey.

**Ms Sales:** Thank you, Madam Chair. As you're all aware, we initiated a live broadcast on Shaw TV of the public meeting held in Lethbridge on October 20. The broadcast went well. I don't know how many of you have seen it, but Shaw did a great job with the broadcast, and it is still accessible on Assembly Online.
Although Shaw isn't able to accurately measure viewership across the entire province at the present time, they do broadcast to about 75 per cent of all Albertans, and they were able to measure viewership for the Calgary area specifically, which brought approximately 6,000 viewers to our live broadcast. The goal of broadcasting live, to my understanding, was to expand the reach of the meeting beyond the host community of Lethbridge. I believe we were successful in achieving this, and I think those numbers do indicate such.
I'm not sure if there are any questions.

**Ms Blakeman:** I was one of the ones that was very concerned about the amount of money we were spending on these public meetings for the number of attendees that we actually got, and I had wanted to move completely to a Skype type of situation or a broadcast situation. Are you able to give us a breakdown now of how much money we spent versus how many people we think we had involved in this or watching it in any way, shape, or form? The number previously was very high for the turnout that we had. If you're telling me that you can verify 6,000 that were watching through Shaw . . .

***11:50***

**Ms Sales:** Yes.

**Ms Blakeman:** So two questions. How much did Shaw cost us? Secondly, are you able to give me an average per participant of the cost that we expended to get that participation?

**Ms Sales:** Okay. Well, I can tell you that the approved cost for the broadcast was $5,500. Unfortunately, because Shaw is not able to meter across the province, they can't tell us exactly how many people were watching all across Alberta. The only number that I have to work with which is accurate is the 6,000 in Calgary. Now, we could extrapolate that chances are that there were other Albertans watching, but I can't guess at that number for you. All I can accurately say is the 6,000. What I can say for sure is that we've never had 6,000 people come to a meeting, so I think that the TV broadcast was a successful way to go, and I think that we did definitely have a lot more participants than usual.

**Ms Blakeman:** I'm sorry. How many were actually on the spot? Sorry to butt in there.

**Ms Sales:** I'm sorry?

**Ms Blakeman:** How many attendees actually were on location?

**Ms Sales:** Actually, to be honest, I don't have the exact number of attendees because once the broadcast started, the lights went out, and it was quite dark. I definitely think it was under five. There was not a very large turnout as far as local participation.

**Ms Blakeman:** Five people came in person to the meeting? Did I hear that right?

**Ms Sales:** Yeah. It was under five. I'm not sure of the exact number.

**Ms Blakeman:** So there were more members of the Heritage Savings Trust Fund Committee than there were audience members?

**Ms Sales:** Yes.

**The Chair:** Yeah. I think, Laurie, you raise some good points. We had a brief discussion afterwards and we will have the discussion in the future about our next public meeting because word got back fairly quickly that Shaw was very successful, and it seemed like we did have a fairly large audience. We also heard some feedback on it that people thought it was quite good. But we were just commenting that night that perhaps next year, seeing that we now have opened up via Shaw – and there were some other possibilities that we talked about at budget time but chose not to start out with. I think there were two other options that we could have really opened up.
But I think you've highlighted what our next big discussion is. What we did say that night is that we could have done all of that in Edmonton, saved all the travel, and still had that kind of success on Shaw. We did wonder about the low number of attendees. However, in talking to some of the local MLAs, what was heavily advertised was the fact that it was going to be covered by Shaw, and they thought perhaps people, the ones that were interested, were just going to watch it on Shaw.
Anyway, Hugh, you wanted to comment on this?

**Mr. MacDonald:** Yes. Ms Blakeman, I'm sure you can appreciate this. At the same time we held the meeting in Lethbridge, the orchestra, the local symphony, was having a concert probably 50 metres down the hall in a different theatre, a much larger one. It was standing room only. It was packed. I went down and talked to some of the people, and they had taken the opportunity to listen to the orchestra. They offered us, after our meeting, while we were waiting for the airplane, an opportunity to listen as well. Some people who had planned to go to our meeting wound up listening to the symphony. You'd be happy with that. It was standing room only, Laurie.

**Ms Blakeman:** I'm sure that proves my point about the value of arts but rather underlines my point about the value of these committees travelling. My concern about this is that I had wanted to dispense with the public meeting, but we were told by Parliamentary Counsel that given the wording of the legislation that was not appropriate. So my question now is: are we now moving to ask for a change in the legislation, or, two, are we going to continue to say that those five people that wish to come from wherever can sit in the back of this room, and we will now embark on something like Skype, which would allow us to have an interaction with the people that are watching? It's one thing for us to televise it; it's another to allow people to be involved in the proceedings. How is this committee moving forward now?

**The Chair:** I think that is a topic for a future meeting, and it will be.

**Ms Blakeman:** How future?

**The Chair:** Well, I would say probably the next meeting, early next year.

I think Tracey raised a really good point. When we had talked about the plans for this year and had taken a look at the last six or eight annual public meetings, we did have attendances of 10, 20, 30. I think 30 was a big one. I don't think we should forget that Tracey has hit a very good point here. Six thousand in Calgary, and I think that at some point somebody had commented that they were thinking somewhere around 20,000 across the province: we've never had anything like that. We've opened up some opportunities, and I think that for our next meeting we can have the discussion, Laurie, and there might be a way to save costs yet go after a larger audience without losing personal participation if that's what's wanted.

**Ms Blakeman:** Well, I'm just wondering, in anticipation of that meeting, which is likely to be: is it possible to ask Tracey to start investigating whatever she thinks might be possible here for interactive? Could she look at Skype and just be prepared to bring some stuff forward to that meeting to help our discussion rather than us getting to a meeting and saying, "Okay; now we need to look at this" and then sending her away and having another meeting so that we can all look at the work? Could we not charge her to examine now?

**The Chair:** Yeah. I think the committee would agree with that because I think that this is on our next committee meeting. Okay. So we'll take that as direction.

**Ms Blakeman:** Cut loose.

**The Chair:** Yeah.

Okay. I have Alana and then Art.

**Ms DeLong:** Actually, I think Laurie brought it up, and I think we're heading in the right direction there. I just wanted to make sure that she did have direction in terms of collecting the information that we're going to be needing to make some decisions in this area.

**The Chair:** Art.

**Mr. Johnston:** Yeah. Mine has been answered, but I just want to say that one of those five may have been the cleaner that kept coming in and out.

**The Chair:** I can't believe you could see him.

Okay. Are there any other questions for Tracey? That's great. We'll pick up that conversation at our next meeting.

I think, Tracey, congratulations are in order because in many respects that was just a different and new success for this committee.

**Ms Sales:** Thank you.

**The Chair:** Okay. The minister has provided – you should all have a memo on the number of website hits on the external heritage fund site. Are there any questions? If not, that is here just for information purposes. Hugh.

**Mr. MacDonald:** Yes. Are we going to get a copy of the latest detailed list of investments held by the Alberta heritage savings trust fund? We usually get that.

**Mrs. Dacyshyn:** I believe that we did provide that to the members by e-mail saying that it's posted on our internal website.

**Mr. MacDonald:** Is that the latest one?

**Mrs. Dacyshyn:** I can't remember. I'll look it up real quick right now and get back to you.

**Mr. MacDonald:** Okay. Thank you.

**Mr. Brown:** The detailed list is only produced annually, so if you have the March 31, 2010, that is the most up to date. It's a very, very time-intensive project, so it is only produced annually. As you can imagine, it's multiple hundreds of pages.

**Mrs. Dacyshyn:** It is posted on the committee's internal website under Documents and Resources and then Miscellaneous. It's a bit hard to find, but it is there.

**The Chair:** Okay. Is there any other business that members would like to raise? I have one – I was going to say a small item. It's actually rather big. If I could have everybody take a look at Keith in the corner here. This is the last standing committee meeting on the calendar for 2010. Keith Metcalfe, our committee room co-ordinator, has worked with the Leg. Assembly Office for seven years, and I understand that Keith is retiring. So on behalf of the committee and, actually, on behalf of everyone thanks for doing a great job. [applause]

Okay. The next meeting will be required following the release of the third-quarter update on the fund, so we'll probably be looking at late February, early March.

Would someone like to move that the meeting be adjourned? Alana. All those in favour? Motion carried.

To everyone here, safe travels and a very Merry Christmas.

[The committee adjourned at 12 p.m.]

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