

GOVERNANCE

The Mandate of the Bank

As Canada's central bank, the Bank is mandated to contribute to the economic well-being of Canadians. It does this by aiming to keep inflation low, stable, and predictable; supplying safe and secure bank notes; promoting a stable and efficient financial system; and by overseeing key clearing and settlement systems. As the Government of Canada's fiscal agent, the Bank manages foreign exchange reserves, the public debt, and treasury activities.

Corporate Governance Framework

The Bank's corporate governance framework is founded on well-defined roles and responsibilities to fulfill its mandate and relies on key elements such as strategic planning, risk management, transparency, and clear accountability for the priorities set by the Bank and for the results achieved.

Central to the Bank's approach to corporate governance is the development of a three-year medium-term plan. The Board of Directors has overall responsibility for approving the strategic direction and the plan itself, and monitors progress of the plan's implementation.

The plan sets out the Bank's strategic priorities and financial plans, includes an integrated analysis of related risks, and provides performance measures aligned with the objectives of the plan. The Board conducts an annual review of the Bank's stewardship to take stock of progress and of the overall achievement of the plan's objectives.

Risk management is a fundamental element of governance. The Bank identifies key areas of risk, based on its responsibilities and strategic priorities. In an annual assessment, senior managers examine business, reputational, financial, operational, security, and disaster-recovery risks. They identify and assess risks that could impede the fulfillment of the Bank's

objectives. Cost-effective mitigation strategies are put into place, monitored by management, and reviewed periodically as part of the internal Audit Department's work plan. The Bank's Audit Department reports to the Audit Committee of the Board and meets with the Committee privately to discuss the effectiveness of the internal controls put in place to mitigate risks. The Board of Directors oversees the entire risk-management process.

The Bank has a Financial Risk Office independent of operations. It monitors and reports on risks and investment performance arising from the management of the government's debt and foreign reserves. The Department of Finance and the Bank have oversight responsibilities for the results of this monitoring.

The Bank also has a detailed business-continuity plan in place. This plan has two main objectives: to provide the public with continuity of critical banking operations and to provide for the safety of Bank staff and the protection of other assets.

Transparency through effective and regular communication is another critical part of the Bank's governance framework. Regular appearances by the Governor and Senior Deputy Governor before committees of the House of Commons and the Senate, together with speeches by senior officials, publications, research material, and reports on the website, serve to demonstrate the Bank's accountability in achieving its public policy objectives. The Bank's website <www.bankofcanada.ca> regularly provides information of interest to the public about Bank activities.

Highlights in 2006

A major accomplishment in 2006 was the approval of the new medium-term plan. Through the process leading up to approval of the plan by the Board, management presented possible strategic priorities for the Board's consideration. After several stages of refinement that took account of the Board's guidance on risks and on the financial framework for the plan, a final version was approved for a three-year term. Key elements of the new plan are discussed later in this report.

In light of developing labour market trends, consideration of issues related to the Bank's compensation strategy were the subject of discussions at the Board and with the Executive Management Committee. The context for these discussions is the Bank's human resource framework, which aims to provide staff with competitive levels of pay related to comparable markets, along with distinctive challenges and opportunities and a superior work environment. These issues will continue to require Board attention in 2007. In response to concerns about workload management, Board requirements and other corporate processes were reviewed to identify opportunities for streamlining with the objective of reducing the overall work effort, while maintaining all the information needed for effective decision making.

As part of its oversight responsibility to monitor the effectiveness of the process for formulating monetary policy, the Board met in private session with Special Adviser Bruce Little, one of Canada's most respected financial

Bank Staff

The Bank's 1,200 staff are critical to its success as a knowledge-based organization. While most of the staff are located at the head office in Ottawa, about 100 work at operations centres in Toronto and Montréal. A small number of staff with expertise in economic, financial market, and currency issues are located at regional offices in Vancouver, Calgary, Toronto, Montréal, and Halifax.

In striving to create a work environment where ideas thrive and knowledge is shared, the Bank works hard to provide opportunities for career development and challenging work. Fundamental to this environment is the Bank's support for bilingualism, employment equity, and a balance between work challenges and personal needs. As with many organizations, Bank staff represent a broad demographic of experience; human resource policies are being reviewed to ensure that the Bank can continue to respond to changing workforce needs and interests. For more information, see *About the Bank* at <www.bankofcanada.ca>.

journalists. Mr. Little's communications experience with macroeconomic issues contributed to discussions of transparency and related issues with the Bank's management during a one-year period ending in August 2006. In 2006, the Board also met with representatives of the International Monetary Fund, who provided additional external views on the Bank's capacity to accomplish its monetary policy objectives.

In keeping with the Bank's objective of maintaining best practices in corporate governance, monitoring of external trends, particularly as they relate to Crown corporation governance, has continued, and the structure of this year's annual report reflects enhancements modelled after the best practices of other institutions. Finally, modifications to accounting practices in response to new standards issued by the Canadian Institute of Chartered Accountants were approved.

Board of Directors

The Board of Directors contributes to the governance of the Bank by overseeing all administrative functions, as well as the process by which the Bank ensures the effective formulation of monetary policy.

In addition to the Governor, who by statute chairs the Board, and the Senior Deputy Governor, the Board is composed of 12 independent Directors and the Deputy Minister of Finance (who has no vote but is an important link to the Department of Finance).

The 12 independent Directors are appointed by the Minister of Finance (with the approval of the Governor-in-Council) for renewable three-year terms. In 2006, five new Directors joined the Board, and orientation meetings with Bank staff were held to familiarize Directors with the functions, operations, and plans of the Bank.

As noted earlier, the Board is responsible for reviewing and approving the Bank's corporate objectives, plans, and budget. The independent Directors are also responsible for appointing the Governor and the Senior Deputy Governor to seven-year terms (with the approval of the Governor-in-Council) and for evaluating their performance. An inherent part of the Board's oversight of management effectiveness is its annual review of the Bank's succession plans to ensure continuity of knowledge for the effective ongoing management of the Bank.

In 2006, the independent Directors elected a new Lead Director, Dr. David Barnard. As Chairperson of the Board's Corporate Governance and Nominating Committee, he oversees the corporate governance practices of the Board and the Bank. The Lead Director chairs private meetings of the independent Directors at each Board meeting and leads the annual Board self-assessment process, a tool that facilitates a full discussion of the Board's practices. Dr. Barnard replaced Spencer Lanthier, who completed two terms as a Director, making notable contributions to the Bank's governance since becoming Lead Director in 2003.

To fulfill its responsibilities of governance and oversight, the Board has several permanent committees. In addition to the Executive Committee, provided for in the Bank of Canada Act, there are committees on corporate governance, human resources and compensation,

audit, planning and budget, and pension. As required, Advisory Groups of several Directors provide a forum for discussing issues of particular interest. Three Advisory Groups currently exist to discuss currency, information technology, and pension matters. The Board forms a Special Committee to direct the recruitment process when a new Governor or Senior Deputy Governor must be chosen.

- Executive Committee: Chair, David Dodge (Governor)
- Corporate Governance and Nominating Committee: Chair, Dr. David Barnard (Lead Director)
- Human Resources and Compensation Committee: Chair, Jocelyne Pelchat
- Audit Committee: Chair, Michael O'Brien
- Planning and Budget Committee: Chair, Jean-Guy Desjardins
- Pension Committee: Chair, Paul Jenkins (Senior Deputy Governor)

Directors are paid according to a fee structure recommended by the government, approved by Governor-in-Council and published in the *Canada Gazette*. For 2006, the aggregate remuneration paid to all independent Directors was \$274,400. This remuneration includes payment of annual retainers and per diems (six Board meetings and those of Advisory Groups and Committees noted above) and participation in other Bank-related activities.

BOARD OF DIRECTORS



David Dodge
Governor
Appointed in 2001



Paul Jenkins
Senior Deputy Governor
Appointed in 2003



Dr. David T. Barnard
Lead Director
President and CEO, iQmedX
Regina, Saskatchewan
Appointed in February 2005



William Black
Corporate Director
Halifax, Nova Scotia
Appointed in October 2006



Philip Deck
Chairman and CEO, MKS Inc.
Toronto, Ontario
Appointed in October 2006



Jean-Guy Desjardins
Chairman and CEO, Centria Inc.
Montréal, Quebec
Appointed in March 2003



Paul D. Dicks
Partner, Benson Myles
St. John's, Newfoundland and Labrador
Appointed in December 2002



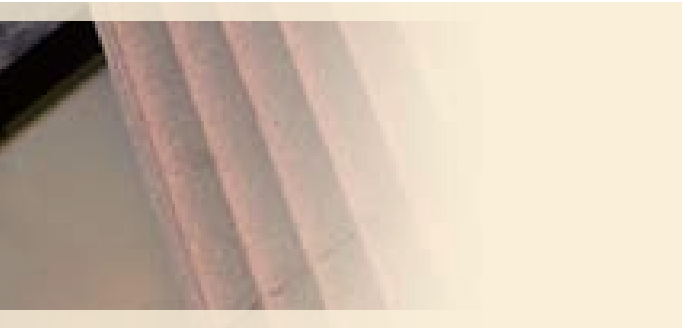
Bonnie DuPont
*Group Vice-President,
 Corporate Resources, Enbridge Inc.
 Calgary, Alberta
 Appointed in October 2006*



Carol Hansell
*Senior Partner
 Davies Ward Phillips & Vineberg LLP
 Toronto, Ontario
 Appointed in October 2006*



Barbara Hislop
*Executive Director
 Variety—The Children's Charity of British Columbia
 Vancouver, British Columbia
 Appointed in March 1998*



Gilles Lepage
*Corporate Director
 Caraquet, New Brunswick
 Appointed in May 2005*



Michael O'Brien
*Corporate Director
 Charlottetown, Prince Edward Island
 Appointed in October 2006*



Jocelyne Pelchat
*President and CEO, Entreprises Pelchat Moïse Inc.
 Sutton, Quebec
 Appointed in February 2005*



Thomas J. Rice
*Chairman, Jovian Capital Corp.
 Winnipeg, Manitoba
 Appointed in June 2005*



Robert Wright
*Deputy Minister of Finance
 Member ex officio*

Governing Council

Under the Bank of Canada Act, the Governor alone is responsible for implementing monetary policy. In practice, however, the Governor shares this responsibility with fellow members of the Bank's Governing Council. The Council works by consensus to formulate, implement, and communicate monetary policy with the support of the Bank's economics and communications departments. A central element of the accountability framework for monetary policy is the agreement between the Bank and the federal government on the inflation-control target. This agreement was renewed on 23 November 2006 for a five-year period

ending 31 December 2011. The inflation target remains the 2 per cent midpoint of a 1 to 3 per cent inflation-control range. Monetary policy decisions on the appropriate setting of the policy interest rate, consistent with delivering the inflation target over the medium term, are normally taken on eight pre-announced fixed dates. The decisions are communicated in press releases and in the *Monetary Policy Report and Update*, which discuss current economic and financial trends in the context of Canada's inflation-control strategy.

The Governing Council is composed of the Governor, Senior Deputy Governor, and the four Deputy Governors.



Governing Council (left to right): David Longworth, Deputy Governor; Tiff Macklem, Deputy Governor; David Dodge, Governor; Sheryl Kennedy, Deputy Governor; Paul Jenkins, Senior Deputy Governor; Pierre Duguay, Deputy Governor



Executive Management Committee (left to right): Sheila Vokey, Chief of the Financial Services Department; David Longworth, Deputy Governor; Tiff Macklem, Deputy Governor; Janet Cosier, Adviser on Strategic Planning and Risk Management; David Dodge, Governor; Mark Jewett, General Counsel/Corporate Secretary; Sheryl Kennedy, Deputy Governor; Paul Jenkins, Senior Deputy Governor; Pierre Duguay, Deputy Governor; Sheila Niven, Chief of the Corporate Services Department

Executive Management Committee

The Bank's Executive Management Committee provides the direction and guidance required to carry out the Bank's responsibilities, oversees all the operations of the Bank, and decides on broad organizational, financial, and strategic issues to be recommended to the Board of Directors for approval.

Financial System Committee

The Financial System Committee reviews issues relating to the domestic and international financial systems, and formulates policy in areas specific to the Bank's responsibilities on matters of general principle, oversight policy, and risk/efficiency trade-offs.

The Committee is composed of all members of the Governing Council, along with the General Counsel/Corporate Secretary; the Adviser, Regulatory Policy; and the Chief of Communications.