Canadian Pacific Railway Limited

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Ticker: CP | Exchange: Toronto Stock Exchange | Index: S&P/TSX Composite | Sector: Railroads | GICS: 20304010 | Meeting Type: Proxy Contest | Meeting Date: 17 May 2012 | Record Date: 22 March 2012 | Meeting ID: 692468

Executive Summary

- Pershing Square Capital Management, which holds 14.2% of outstanding shares, has nominated a slate of 7 dissident candidates for the board. Pershing Square's CEO William Ackman has been nominated on both the management and the dissident slate.
- If successful in obtaining board representation, the dissidents would seek to replace the current CEO. Though Pershing Square has publicly indicated it would be open to running an executive search process, it has also already recruited former Canadian National Railway CEO Hunter Harrison to take the CEO role.
- Both management and the dissidents have listed all 22 nominees for the 16 available seats on their respective proxy cards, making each one a universal ballot. Shareholders may only vote for up to 16 nominees, however.

Financial Performance

	1-year	3-year	5-year
Company TSR (%)	8.90	21.30	4.21
GICS 2030 TSR (%)	4.15	24.72	0.78
S&P/TSX Composite TSR (%)	-8.75	13.18	1.28

TSRs are as of closest month end to company's FYE. More information

Agenda and Recommendations

Canada Policy

Item	Code	Proposal	Mgt. Rec.	ISS Rec.	Focus
Management Proxy (White Card)					
1	M0101	Ratify Deloitte & Touche LLP as Auditors	FOR	DONOTVOTE	❖
2	M0550	Advisory Vote on Executive Compensation Approach	FOR	DONOTVOTE	❖
Management Director Nominees (Shareholders May Only vote FOR 16 out of 22 Director Nominees)					
3.1	M0299	Elect Director John E. Cleghorn	FOR	DONOTVOTE	❖
3.2	M0299	Elect Director Tim W. Faithfull	FOR	DONOTVOTE	❖
3.3	M0299	Elect Director Richard L. George	FOR	DONOTVOTE	❖
3.4	M0299	Elect Director Frederic J. Green	FOR	DONOTVOTE	❖
3.5	M0299	Elect Director Edmond L. Harris	FOR	DONOTVOTE	❖
3.6	M0299	Elect Director Krystyna T. Hoeg	FOR	DONOTVOTE	❖
3.7	M0299	Elect Director Tony L. Ingram	FOR	DONOTVOTE	❖
3.8	M0299	Elect Director Richard C. Kelly	FOR	DONOTVOTE	❖

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Item	Code	Proposal	Mgt. Rec.	ISS Rec.	Focus
3.9	M0299	Elect Director Hon. John P. Manley	FOR	DONOTVOTE	❖
3.10	M0299	Elect Director Linda J. Morgan	FOR	DONOTVOTE	❖
3.11	M0299	Elect Director Madeleine Paquin	FOR	DONOTVOTE	❖
3.12	M0299	Elect Director Michael E.J. Phelps	FOR	DONOTVOTE	❖
3.13	M0299	Elect Director Roger Phillips	FOR	DONOTVOTE	❖
3.14	M0299	Elect Director David W. Raisbeck	FOR	DONOTVOTE	❖
3.15	M0299	Elect Director Hartley T. Richardson	FOR	DONOTVOTE	❖
3.16	M0299	Elect Director William A. Ackman	FOR	DONOTVOTE	❖
Shareholder Director Nominees					
3.17	S0250	Elect Shareholder Nominee Gary F. Colter	FOR	DONOTVOTE	❖
3.18	S0250	Elect Shareholder Nominee Paul G. Haggis	WITHHOLD	DONOTVOTE	❖
3.19	S0250	Elect Shareholder Nominee Paul C. Hilal	WITHHOLD	DONOTVOTE	❖
3.20	S0250	Elect Shareholder Nominee Rebecca MacDonald	WITHHOLD	DONOTVOTE	❖
3.21	S0250	Elect Shareholder Nominee Anthony R. Melman	WITHHOLD	DONOTVOTE	❖
3.22	S0250	Elect Shareholder Nominee Stephen C. Tobias	WITHHOLD	DONOTVOTE	❖
Dissident Proxy (Blue Card)					
1	M0101	Ratify Deloitte & Touche LLP as Auditors	FOR	FOR	
2	M0550	Advisory Vote on Executive Compensation Approach	AGAINST	FOR	❖
Shareholder Director Nominees (Shareholders May Only vote FOR 16 out of 22 Director Nominees)					
3.1	S0299	Elect Director William A. Ackman	FOR	FOR	
3.2	S0299	Elect Director Gary F. Colter	FOR	FOR	
3.3	S0299	Elect Director Paul G. Haggis	FOR	FOR	
3.4	S0299	Elect Director Paul C. Hilal	FOR	FOR	
3.5	S0299	Elect Director Rebecca MacDonald	FOR	FOR	
3.6	S0299	Elect Director Anthony R. Melman	FOR	FOR	
3.7	S0299	Elect Director Stephen C. Tobias	FOR	FOR	
Management Director Nominees					
3.8	S0299	Elect Director John E. Cleghorn	WITHHOLD	WITHHOLD	
3.9	S0299	Elect Director Tim W. Faithful	WITHHOLD	WITHHOLD	
3.10	S0299	Elect Director Richard L. George	WITHHOLD	FOR	❖
3.11	S0299	Elect Director Frederic J. Green	WITHHOLD	WITHHOLD	
3.12	S0299	Elect Director Edmond L. Harris	WITHHOLD	WITHHOLD	
3.13	S0299	Elect Director Krystyna T. Hoeg	WITHHOLD	FOR	❖
3.14	S0299	Elect Director Tony L. Ingram	WITHHOLD	FOR	❖
3.15	S0299	Elect Director Richard C. Kelly	WITHHOLD	FOR	❖
3.16	S0299	Elect Director Hon. John P. Manley	WITHHOLD	FOR	❖
3.17	S0299	Elect Director Linda J. Morgan	WITHHOLD	FOR	❖
3.18	S0299	Elect Director Madeleine Paquin	WITHHOLD	FOR	❖
3.19	S0299	Elect Director Michael E.J. Phelps	WITHHOLD	WITHHOLD	
3.20	S0299	Elect Director Roger Phillips	WITHHOLD	WITHHOLD	
3.21	S0299	Elect Director David W. Raisbeck	WITHHOLD	FOR	❖
3.22	S0299	Elect Director Hartley T. Richardson	WITHHOLD	FOR	❖

❖Recommendations against management | ● Items deserving attention due to contentious issues or controversy

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Financial Profile

Business Description

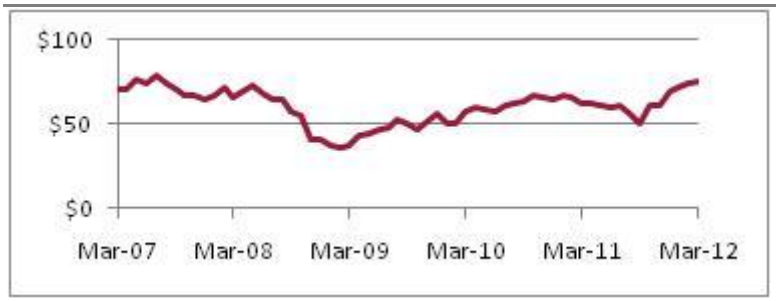
Canadian Pacific was incorporated over 125 years ago to build the transcontinental railway in Canada. The company is still active in the transportation sector providing rail and intermodal freight transportation in Canada and the United States.

Company Snapshot

Industry: Road & Rail (GICS 20304010)	
Market Cap	$11,731.7M
Shares Outstanding	170.0M
YTD Performance	13.3%
Closing Price	$69.01
EPS	$3.37
Book Value/share	$27.35
Sales/share	$30.45
Annual Dividend	$1.17
Dividend Yield	1.7%
Price to Earnings	20.5
Price to book value	2.5
Price to cash flow	11.1
Price to sales	2.3

Data as of fiscal year-end. YTD Performance from last FY end to meeting record date.

Stock Performance



Historical Financial Performance

($ millions)

Profit & Loss	**2011**	**2010**	**2009**
Revenue	5,177	4,982	4,303
Operating Income after Dep.	967	1,116	900
Net Income	570	651	612
EBITDA	1,457	1,606	1,389
Cash Flow	**2011**	**2010**	**2009**
Operating Activities ($ Flow)	512	502	552
Total cash from investing	-1,044	-636	-459
Total cash from financing	217	-168	489
Net change in cash	-314	-318	562

Comparative Performance

	CP	**CNR**	**BBD.B**	**CTC.A**	**MX**	**STN**
Gross Margin	28.1%	46.3%	17.6%	29.5%	32.7%	55.4%
Profit Margin	13.5%	37.2%	5.7%	6.1%	10.9%	3.6%
Operating Margin	18.7%	36.5%	6.5%	7.3%	13.2%	10.9%
EBITDA Margin	28.1%	46.3%	8.3%	10.1%	19.2%	14.4%
Return on Equity	12.3%	23.0%	278.1%	10.6%	14.3%	2.0%
Return on Investment	6.1%	14.4%	15.0%	6.9%	8.7%	1.5%
Return on Assets	4.0%	9.4%	3.4%	3.8%	5.9%	1.0%
P/E	20.5	14.7	8.5	11.5	10.6	98.5
Debt/Assets	33.8	25.3	20.7	28.2	28.5	22.3
Debt/Equity	102.6	61.6	773.2	79.0	68.8	47.2
Total Return	**CP**	**CNR**	**BBD.B**	**CTC.A**	**MX**	**STN**
1 Yr TSR	8.90%	22.91%	-17.43%	-1.58%	-20.90%	-0.58%
3 Yr TSR	21.30%	23.62%	-0.87%	16.83%	23.45%	-2.94%
5 Yr TSR	4.21%	11.84%	2.06%	0.02%	-3.12%	1.77%

Peer Companies: BBD.B: Bombardier | CNR: Canadian National Railway Company | CTC.A: Canadian Tire Corporation, Limited | MX: Methanex | STN: Stantec Source: Standard & Poor's Compustat Xpressfeed.

Figures reported in $(CAD). Compustat data is "standardized data" not "as reported" so there may be a difference from what is reported in company filings. Compustat standardizes the original filings to allow for accurate comparison across companies and industries. For a list of frequently asked questions, go to http://www.issgovernance.com/policy/CompanyFinancialsFAQ

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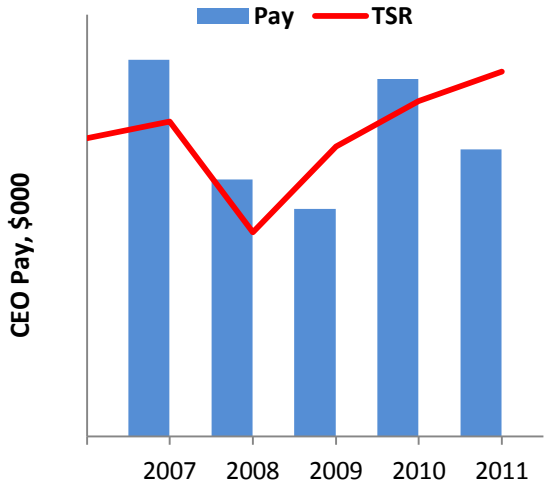
Compensation Profile

Overview of CEO Pay

Pay vs. TSR



	2007	2008	2009	2010	2011
Pay($000)	6,930	4,734	4,194	6,578	5,285
Indexed TSR	105.6	68.5	97.2	112.5	122.3
CEO	Green	Green	Green	Green	Green

Indexed TSR represents the cumulative total return of the company's stock for a five-year fiscal period based on a $100 investment on the first year, including the reinvestment of dividends.
Executive compensation disclosure requirements changed in FY 2008 and comparable historical values for 2006 and 2007 may not be available.

	2011	% Change	2010
CEO Name	Frederic J. Green		Frederic J. Green
Base salary	985,873	6.44	926,250
Annual Bonus	0	-100	1,665,469
Long term Non-equity Incentives	0	0	0
Share-based Awards	1,591,498	20.37	1,322,182
Option Awards	1,591,368	20.44	1,321,261
Pension	1,026,000	-18.44	1,258,000
All Other Compensation	90,339	6.59	84,756
Total Compensation	5,285,078	-19.65	6,577,918
% Pay at Risk*	60.22	-8.06	65.51

*Pay at Risk is defined as sum of short-term and long-term incentives divided by Total Compensation

- No short-term incentive awards were granted in 2011 as the Corporate target (Operating Income) did not meet the minimum hurdle
- CEO's 2009 PSU award with a grant date value of $1,119,946, vested on Dec. 31, 2011; company's performance, share price of $63.12, and re-invest dividends, resulted in a payout of $2,755,126.
- During the year, the Compensation Committee reviewed the CEO's target and actual compensation. Green's total compensation was at the 50th percentile of CEOs in the Comparator Group and below the 25th percentile of CEOs of the other Class I Railroads group. Following the review, Green's 2011 targeted compensation was positioned at the 27th percentile of the other Class I Railroads, which resulted in an increase from $4.6 million to $5.5 million.

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Vote Results for Annual Meeting 12 May 2011

Proposal	Mgmt Rec	Disclosed Result	% For	Focus**
1 Ratify Deloitte & Touche LLP as Auditors	For	Approved	99.87	
2.1 Elect John E. Cleghorn as Director	For	Approved	99.48	
2.2 Elect Tim W. Faithfull as Director	For	Approved	99.82	
2.3 Elect Richard L. George as Director	For	Approved	99.69	
2.4 Elect Frederic J. Green as Director	For	Approved	99.56	
2.5 Elect Krystyna T. Hoeg as Director	For	Approved	99.36	
2.6 Elect Richard C. Kelly as Director	For	Approved	99.39	
2.7 Elect John P. Manley as Director	For	Approved	99.31	
2.8 Elect Linda J. Morgan as Director	For	Approved	99.84	
2.9 Elect Madeleine Paquin as Director	For	Approved	99.35	
2.10 Elect Michael E. J. Phelps as Director	For	Approved	99.33	
2.11 Elect Roger Phillips as Director	For	Approved	99.70	
2.12 Elect David W. Raisbeck as Director	For	Approved	99.83	
2.13 Elect Hartley T. Richardson as Director	For	Approved	99.03	
3 Approve Shareholder Rights Plan	For	Approved	97.42	
4 Re-approve Stock Option Incentive Plan	For	Approved	87.99	
5 Advisory Vote on Executive Compensation Approach	For	Approved	97.03	

**Items with a majority of votes cast FOR shareholder proposal or AGAINST management proposal or director election

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Board Profile

Vote standard: The company has a plurality vote standard for the election of directors, and has a director resignation policy in its governance guidelines.

Director Independence & Affiliations

Executive Directors

On Ballot	Name	Affiliation	ISS Classification	Atten-dance	Age	Tenure	Term Ends	Outside Boards	Outside CEO	Key Committees Audit	Key Committees Comp	Key Committees Nom	Key Committees Gov
☑	Frederic J. Green	CEO	Insider		55	6	2013	0					

Non-Executive Directors

On Ballot	Name	Affiliation	ISS Classification	Atten-dance	Age	Tenure	Term Ends	Outside Boards	Outside CEO	Key Committees Audit	Key Committees Comp	Key Committees Nom	Key Committees Gov
☑	John E. Cleghorn	Chair	Independent Outsider		70	11	2013	1				M	M
☑	William A. Ackman		Independent Outsider		45	0*	2013	0					
☑	Timothy W. Faithfull		Independent Outsider		67	9	2013	3			M	M	M
☑	Richard L. George		Independent Outsider		61	1	2013	2	x		M		
☑	Edmond L. Harris		Affiliated Outsider		62	1*	2013	0					
☑	Krystyna T. Hoeg		Independent Outsider		62	5	2013	3		F			
☑	Tony L. Ingram		Independent Outsider		65	1*	2013	0			M		
☑	Richard C. Kelly		Independent Outsider		65	4	2013	0		C F		M	M
☑	John P. Manley		Independent Outsider		62	6	2013	2		F		M	M
☑	Linda J. Morgan		Independent Outsider		59	6	2013	0		F			
☑	Madeleine Paquin		Independent Outsider		49	11	2013	1	x		M		
☑	Michael E. J. Phelps		Independent Outsider		64	11	2013	3			C	M	M
☑	Roger Phillips		Independent Outsider		72	11	2013	1		F		C	C
☑	David W. Raisbeck		Independent Outsider		62	3	2013	2			M		
☑	Hartley T. Richardson		Independent Outsider		57	6	2013	2		F	M		
				Average:	61	6				100% indep	100% indep	100% indep	100% indep

M = Member | C = Chair
F = Financial Expert

Director Notes

Edmond L. Harris	Edmond L. Harris served as the company's EVP and COO of the company until April 2011 and acted as a consultant to the company in 2011.

* = has not been previously presented to shareholders for election

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Board and Committee Summary

	Members	Independence	Meetings
Full Board	16	88%	12
Audit	6	100%	11
Compensation	7	100%	4
Nomination	6	100%	9
Governance	6	100%	9

Director Employment & Compensation

Name	Primary Employment	Outside Boards	Total Compensation	Shares Held (000)	DSUs (000)	Options (000)	Voting power
John E. Cleghorn	Accountant	Molson Coors Brewing Company	342,675	19	37	4	<1%
Frederic J. Green	CEO, President - Canadian Pacific Railway Limited	--	0	35	51	927	<1%
William A. Ackman	Financial Services		0	24,160	0	0	14.14
Timothy W. Faithfull	Other	TransAlta Corporation, AMEC plc, Canadian Natural Resources Limited	201,776	1	30	0	<1%
Richard L. George	CEO - Suncor Energy Inc	Suncor Energy Inc., Royal Bank of Canada	187,307	10	3	0	<1%
Edmond L. Harris	Consultant	--	98,910	0	2	55	0.00
Krystyna T. Hoeg	Prof Director	Imperial Oil Limited, Sun Life Financial Inc., Shoppers Drug Mart Corporation	192,500	0	16	0	0.00
Tony L. Ingram	Retired	--	98,910	0	2	0	0.00
Richard C. Kelly	Retired	--	209,070	0	11	0	0.00
John P. Manley	Other	Canadian Imperial Bank of Commerce, CAE Inc.	219,500	0	18	0	0.00
Linda J. Morgan	Attorney/Counsel	--	190,402	0	20	0	0.00
Madeleine Paquin	CEO, President - Logistec Corporation	Logistec Corporation	180,000	7	23	4	<1%
Michael E. J. Phelps	Prof Director	Marathon Oil Corporation, Spectra Energy Corp, Prodigy Gold Inc.	207,000	20	19	4	<1%
Roger Phillips	Prof Director	Cliffs Natural Resources Inc.	218,000	7	37	4	<1%
David W. Raisbeck	Prof Director	Eastman Chemical Company, Cardinal Health, Inc.	181,005	0	9	0	0.00
Hartley T. Richardson	Other	Zalicus Inc., GMP Capital Inc.	182,225	15	19	0	<1%
SUMMARY		Average # of Outside Boards: 1.9				Directors Holding Stock: 62%	

Figures in local currency.

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Meeting Agenda and Proposals

Management Proxy (White Card)

Items 1-3.22 DONOTVOTE

Vote Recommendation

DO NOT VOTE – see analysis on the dissident card for additional information.

Background Information

Policies: Ratify Auditors (TSX)

Vote Requirement: Majority of votes cast

Discussion

See analysis on the dissident card for additional information.

Dissident Proxy (Blue Card)

Item 1. Ratify Deloitte & Touche LLP as Auditors FOR

Vote Recommendation

A vote FOR the ratification of the company's auditors is warranted.

Background Information

Policies: Ratify Auditors (TSX)

Vote Requirement: Majority of votes cast

Discussion

Proposal Ratify Deloitte & Touche LLP as auditors.

Auditor	Deloitte & Touche
Auditor Tenure	1 year
Audit Fees	$1,612,600
Audit-Related Fees	$251,000
*Tax Compliance/Preparation**	$50,000
Other Fees	$300,000
Percentage of total fees attributable to non-audit ("other") fees	13.55 percent

Note: Tax fees were for professional services related to tax compliance, tax planning and tax advice. These services consisted of: tax compliance including the review of tax returns; assistance with questions regarding corporate tax audits; tax planning and advisory services relating to common forms of domestic and international taxation (i.e. income tax, capital tax, goods and services tax, and valued added tax); and access fees for taxation database resources.

The auditor's report contained in the annual report is unqualified, meaning that, in the opinion of the auditor, the company's financial statements are fairly presented in accordance with generally accepted accounting principles. The auditor also opined that the company maintained effective internal control over financial reporting as of Dec. 31, 2011 based on criteria established in Internal Control Integrated Framework issued by COSO.

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Item 2. Advisory Vote on Executive Compensation Approach FOR

Vote Recommendation

A vote FOR this non-binding advisory vote is warranted as there are no egregious issues have been identified at this time.

Background Information

Policies: Management Say on Pay (TSX)

Vote Requirement: Majority of votes cast

Executive Summary

Evaluation Component	Level of Concern
Pay for Performance Evaluation	**Low**
Pay Practices	**Low**
Board Communication & Responsiveness	**Low**
Prior Year's Vote Result	97.03% FOR

Discussion

ISS utilizes a global framework when evaluating management-proposed advisory votes pay programs across several markets. For Canadian companies, this involves a case-by-case analysis, under three broad categories: Pay for Performance, Pay Practices and Board Communication and Responsiveness. The goal of this analysis is to identify companies whose boards have failed to demonstrate good stewardship of investors' interests regarding executive compensation practices.

Proposal

BE IT RESOLVED THAT: On an advisory basis and not to diminish the role and responsibilities of the Board of Directors, that the Shareholders accept the approach to executive compensation disclosed in the Proxy Circular delivered in advance of the 2012 AGM.

I. Pay for Performance Evaluation Concern: Low

Incentive Programs Short Term Incentives

CEOs Performance Metrics(weighting)	Corporate Metrics (75%) Individual Performance (25%)
CEOs Last FY Corporate Metrics	Metric: Operating Income; 2011 Target: $1,270 million; 2011 Actual: 990 million; Target Achieved: no
CEO's Individual Metrics	Based on Safety, Growth and Profitability, Leadership, and Customer Service measures. Targets were deemed "Achieved",
Discretionary Component?	No
Discretionary Bonuses Paid to NEOs in last FY?	No
Payout form	Cash but executives can elect to receive all or a portion in the form of DSUs
Change in metrics/ goals?	2011 Corporate target was set 28% higher than 2010 target
CEO's last FY award Target	100% of salary, maximum award capped at 200% of salary
Future Performance Metrics	Not disclosed

Comment: As the Corporate target of Operating Income did not meet the minimum hurdle, no awards were paid out under the plan in 2011.

Incentive Programs Long-Term Incentives

Award type(s)	Options and Performance Share Units (PSUs)

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Vesting provisions	Regular Options vest 50% on each of the second and third grant date anniversaries Performance-Contingent Options (granted prior to 2009) must achieve pre-set Operating Ratio targets to vest, or else they are cancelled. 100% of 2007 PC options and 50% of the 2008 PC options have been cancelled. PSUs have a 3 year performance period
Performance-based awards?	Yes. PSUs vest depending on two performance measures weighted equally: Return on Capital Employed and Relative TR compared to the S&P/TSX60 Index. If thresholds of both metrics are not met, no awards vest.

Current Performance Metrics/Goals for Performance Period 2011-2013

Metric	Threshold	Target	Exceptional
2013 ROCE	9.6%	10.8%	12.0%
TSR Relative to Index	-2%	0%	4%
Payout Level Schedule	50%	100%	200%

Current Performance Cycle	3 years
Performance Metrics Results Adjusted?	No
Did the company reprice options in last FY?	No
Equity Pay Mix	CEO: 50% Options, 50% PSUs

Comment: The three year performance period for the 2009 grant of PSUs ended Dec. 31, 2011 and the company's actual results below generated a payout of $2,755,126 for the CEO. The Option Plan was amended in February 2012 to incorporate a double trigger on the change of control provision, which will apply to all future grants of options.

Metric	Threshold	Target	Exceptional	Actual Result	Payout Level Achieved
2013 ROCE	9.6%	10.8%	12.0%	**7.4%**	0%
TSR Relative to Index	-2%	0%	4%	**11.4%**	200%

Pay for Performance Analysis

As shown in the chart below, the company's 3-year total shareholder returns (TSR) were below the median TSR of its 4-digit GICS group. However over the shorter one-year and longer five-year period, the company's TSR was above.

Total Shareholder Return (TSR) Comparison (%, annualized for the periods ending Dec. 31, 2011)

	1-Year TSR	3-Year TSR	5-Year TSR
Company	8.90	21.30	4.21
S&P/TSX Composite Index	-8.75	13.18	1.28
S&P/TSX (Industrials Sub) Index	4.15	15.61	5.04
GICS Group (2030) Median	4.15	24.72	0.78

Source: Xpressfeed / Bloomberg

CEO Tenure:	6 years
Total Compensation:	$5,285,078
% Change in Total Compensation:	-19.65%
Pay-for-Performance Disconnect:	No

II. Pay Practices Concern: Low

Assessment of Pay Practices

The company does not have any excessive employment contracts, loans, change-in-control agreements, or perquisites with any of the Named Executive Officers. Below are certain items of note.

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Practice	Concern
Supplemental Executive Retirement Plan	As of 2010 additional benefits are no longer available to new participants in the SERP. Previously, mid-career hires had received additional credits that vested over 5 years. A new Defined Contribution plan was introduced in 2010 and the Defined Benefit plan was closed to new non-union hires. In 2011, CEO's target bonus percentage used in the calculation of his pension was capped at 100%. His annual pension benefit at age 65 estimated at $1,220,000 on Dec. 31, 2011.
Internal Pay Disparity	CEO is paid 1.7x the second highest paid executive, K.B. McQuade, EVP and CFO
Matching under DSU plan	In order to aid executives in reaching their ownership requirements, for the first six months of an individual's appointment to a new executive officer's role or increase in the ownership threshold, the company will match 1 DSU for every 3 DSUs or shares acquired by the individual. After this period, for another 4.5 years, the company will match 1 DSU for every 4 DSUs or shares acquired by the individual. Matching DSU vest if the underlying shares or DSUs are held for 3 years. DSUs can be redeemed only after termination of employment. CP match is capped at the minimum ownership guidelines.

CEO Severance/Change in Control Arrangement

Trigger:	Double Trigger
Multiple:	3x
Basis:	Base Salary + Bonus
Treatment of Equity:	Options, DSUs and PSUs vest immediately upon a change of control. PSUs vest on target and are prorated based on period to the effective date of CIC
Total Estimated CIC Severance:	$17,691,802 as follows • Severance Payment: $6,000,000 • Additional Retirement Benefits: $5,623,000 • Other Benefits: $206,296 • Early Vesting of Equity Awards: $5,862,506

Comment: The CEO's severance multiple, at 3xs salary plus bonus is considered excessive. Best market practice in the Canadian market dictates a change in control multiple of 2xs.

Compensation and Risk Alignment Discussion

During 2011, the Committee reviewed compensation policy risk issues identified in consultation with the Corporation's compensation consultant. As a result, new disclosure practices were introduced and others expanded to align with the Canadian Coalition for Good Governance disclosure best practices.

Risk Mitigators

Clawback Policy	Policy adopted 2011
Stress testing	CEO's compensation arrangements are stress-tested to ensure they work as expected
Personal Hedging	Employees and directors prohibited from purchasing financial instruments that are designed to hedge or offset a decrease in market value of equity securities of CP granted as compensation or held, directly or indirectly.
CEO Stock Ownership guideline	4 times salary
Bonus Deferrals	Executives may elect to defer some or all of their bonuses into DSUs

Company Peer Group

Number of Peer Groups	Two Peer groups (executive and director)
Number of Peer Group constituents:	55 named Canadian issuers with annual revenues exceeding $1 billion

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Compensation Benchmarking Target:	Total compensation positioned between 50th and 75th percentile

Comment: Beginning in 2011, Class 1 Railroads were also used as a secondary reference point to ensure appropriate compensation levels for select positions.

Cost of Management Ratio (total aggregate compensation for top five Named Executive Officers as a percentage of NIAT)

	2011	2010	2009	2008	2007
Ratio using Total Aggregate NEO Compensation	2.5%	2.4%	1.8%	1.6%	1.5%
Ratio using Total Aggregate NEO Compensation less Pension value	1.7%	2.0%	1.8%	1.4%	1.1%

III. Board Communication and Responsiveness Concern: Low

Clarity of Compensation Disclosure

The CD&A highlighted major changes to the compensation program over the past year in a concise manner.

Compensation Rationale

The Compensation Committee believes the company's executive compensation program focuses senior executives on executing on the company's Multi-Year Plan, which aims to generate superior returns for shareholders through continuous improvement in financial and operating performance, while remaining true to the vision of being the safest and most fluid railway in North America. To further support the continued focus on improving operating ratio to between 70 and 72 for 2014, both the annual incentive plan and long-term incentive plan will re-introduce operating ratio as a performance measure beginning in 2012.

Disclosure of Fees paid to Compensation Committee Advisor

	2011	2010
Compensation Committee Advisor:	Towers Watson	Towers Watson
Committee/ Board Mandated Fees:	$228,353	$146,000
Company Mandated Fees:	$1,746,781	$2,178,000
Percentage of total fees attributable to company mandate:	88%	94%

Comment: The breakdown of fees paid to the external compensation advisor show a high proportion of advice and/or services provided under the company mandate in comparison to the committee/board mandate. The services provided under the Company mandate include; actuarial, asset consulting and benefit services. The Committee applies a financial independence test and considers the advisor independent if the fees earned from the Corporation do not exceed 1% of the advisor's annual revenue. Management must receive pre-approval from the Committee for any request related to executive compensation services, but not in respect of any other service provided by Towers Watson.

Board's Responsiveness to Investors

Board Responsiveness	Non-binding Say on Pay adopted in 2011, following 2010 shareholder proposal which was subsequently withdrawn
Prior Year MSOP vote	97.03% FOR
Shareholder Communication	Shareholders are able to communicate with the Chairman of the Board directly through written or electronic means

Analysis

I. Pay for Performance

There is no pay for performance disconnect as defined by ISS proxy guidelines.

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II. Pay Practices

As referenced in the Pay Practices section above there are problematic pay practices as highlighted below.

- Under the bonus deferral program, executives may defer their bonuses into DSUs and the company will match a certain percentage of the executives' contribution for the first 5 years. ISS prefers that executives defer bonuses into DSUs in order to achieve their ownership thresholds from their own compensation, and not simply be "given" additional DSUs from the company in order to reach these thresholds.
- The CEO's change in control severance multiple at 3xs salary plus bonus, is excessive. A multiple of 2xs is considered best practice in the Canadian market

III. Board Communication and Responsiveness

The high proportion of fees paid to the external compensation advisor under the Company Mandate raises questions about the independence of advice provided under the Board Mandate.

Conclusion

The board has demonstrated good stewardship of investors' interests regarding executive compensation practices. Upon review of the company's compensation programs and practices ISS finds no significant issues of concern; therefore a vote FOR this proposal is warranted.

Nominees (Shareholders May Only Vote FOR 16 of 22 Director Nominees)

Items 3.1 – 3.22. Elect Directors – Dissident Slate SPLIT

Vote Recommendation

As the dissidents have made a compelling case that change at the board level is necessary, votes FOR dissident nominees Ackman, MacDonald, Haggis, Coulter, Melman, Tobias and Hilal is warranted.

Additionally, votes FOR management nominees George, Ingram, Paquin, Morgan, Manley, Hoeg, Kelly, Richardson and Raisbeck are warranted to optimize the new board. Shareholders should WITHHOLD votes from the remaining 6 management nominees.

Background Information

Policies: Contested Election (TSX)

Vote Requirement: Majority of votes cast

Background

Pershing Square Capital Management, which beneficially owns 14.2% of outstanding shares, has proposed a slate of 7 nominees to the now-16 member board. If successful, the Pershing nominees intend, among other things, to conduct a search for a new CEO to replace current CEO Fred Green—although Pershing Square's candidate, former Canadian National CEO Hunter Harrison, is the presumptive nominee.

The company has offered Pershing Square CEO Bill Ackman a seat on the board as a settlement. Though Pershing Square declined, the board has nominated Ackman on its slate of 16.

Each side has adopted a "universal ballot" format, through which every board nominee—the 15 incumbent directors, Ackman (who appears on both slates), and the 6 additional Pershing Square nominees—are included on each proxy card. Shareholders can vote for up to 16 of the total nominees, without regard to slate.

Key Events

Oct 28, 2011—Pershing Square reports beneficial ownership of 20.7 million shares (12.2%), including 2.7 million shares underlying call options.

Dec. 15—CP board expands by adding former railroad executives Tony Ingram and Ed Harris. Harris had also briefly served

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as CP's COO. CP also offers Pershing Square CEO Bill Ackman a newly-created seat. Pershing, seeking 2 seats and a change in CEO, declines settlement offer.

Dec. 30—*The Globe and Mail* reports that Pershing (now a 14.2% holder) is pushing for former Canadian National Railway (CNR) CEO Hunter Harrison to replace current CP CEO Fred Green.

Jan. 3, 2012—In open letters to one another, CP publicly rebukes Pershing's CEO replacement proposal, and Pershing—asserting it did not leak its proposal—notes CP's Chairman had requested Pershing arrange a meeting with Harrison.

Jan. 9—Bloomberg reports Pershing will wage proxy fight.

CP files open letter to shareholders highlighting its business plan (targeting operating ratio in "low 70s"), voicing unanimous support for management team, and criticizing Pershing for not presenting a detailed plan.

Jan. 17—CP announces 2012 capital plan: $1.1 billion for infrastructure renewal, network enhancements, and other expansion projects.

Jan. 23—Pershing requisitions a shareholder meeting, will propose 5 candidates (subsequently raised to 7 candidates) to 16-seat board.

Wall Street Journal reports CNR has suspended pension benefits to and filed breach of contract suit against its former CEO. Harrison's lawyer, pointing out two-year non-compete expired in 2011, labels suit "frivolous."

Jan. 26—CP announces 4Q results: net income C$1.30 per share, C$0.21 per share higher than prior year quarter—but includes C$0.22 per share income tax benefit.

Feb. 6—Pershing hosts web-based town hall to introduce nominees, discuss its plan for CP; believes plan could take share price to $140 by 2015.

Mar. 7—CP sends letter to shareholders claiming a board overhaul would "put at severe risk" the railroad's turnaround plan; highlights board's execution on its multi-year plan, series of high-profile commercial agreements. Investor presentation 20 days later contends customers will flee in droves is Harrison appointed CEO.

Mar. 22—Record date.

Mar. 27—During Investor Day, CP reveals a board-commissioned consultant has determined structural disadvantages vs. CNR explain 670 basis points of durable disadvantage in operating ratio (OR). Study also declares Pershing Square's targeted OR of 65% "not possible by 2015," but ratifies CP's plan to achieve OR of 70-72 by 2014.

Apr. 20—CP announces 1Q results: net income of C$0.83 per share, operating ratio at 80.1%.

May 17—Shareholder meeting.

Dissident Critique

The dissidents contend that a complacent board, demanding little accountability from a CEO already out of his depth, has allowed the company to miss out on the revolution in railroading over the past decade which dramatically improved the operating performance—and shareholder returns—of the 5 other major North American railways.

Poor performance is clear, they point out. For the five years ending Sept. 22, 2011, the date the dissidents began accumulating their more than 14% of shares, the company had a negative 18% total return to shareholders. The nearest peer among the other 5 Class 1 North American railways was 40 percentage points higher, at 22% for the period, and the best performing railways over that period—reflecting their embrace of the new operating model of "Precision Railroading," were up as much as 93%. The company's Operating Ratio (OR)—total expenses divided by revenue, the industry's key measure of operating efficiency and fiscal health—actually worsened over the 6-year tenure of the current CEO, even as peers rapidly improved theirs. Ranked in the middle of the pack when he took office in 2006, it had settled in to last place by 2008—then watched complacently as the pack continued to pull away.

Despite this evidence the industry had reached a new understanding of how a railroad creates value, for customers as well as shareholders—neither the CEO nor the board elected to hold him accountable moved to address the real issues. Instead the company evolved a self-soothing mythology to explain why its circumstances were different, and its results acceptable. 'The company commands lower pricing versus CNR,' for example: adjusted for length of haul (effectively, for the fact that much of the cost the railway incurs is in the terminals, and much of the profitability comes on the track between terminals),

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the dissidents point out the deficit is modest. Despite having significantly longer hauls than CNR—which should have conferred a cost advantage—the company operated at a unit cost disadvantage to CNR, and the disadvantage—a net push when the CEO took office—had jumped substantially over his tenure as its inefficiency versus peers grew more pronounced.

Poor asset utilization was part of the issue: CP moved about 71% of Canadian freight tonnage in 2005 and 2010. Where that required 55% of freight cars and 81% of locomotives in 2005, though, CNR's ongoing improvements coupled with CP's lack of progress meant it required 80% of the freight cars, and 93% of the locomotives, to move its share of freight in 2010. But management itself was exacerbating the problem: despite locomotive utilization 23% lower than CNR's in 2010, and a blanket statement from its then-COO (now a director) that the company "doesn't need more locomotives," management developed a strategic plan that called for 91 new locomotives in 2011 and Q1 2012.

Meanwhile inferior service levels—left unaddressed, even as competitors continued to improve—were making themselves felt on the revenue side of the business equation. This was true both in terms of revenue "yield" and market share, and particularly in segments, such as intermodal transportation, where substitutes for rail shipping were more readily available. This vicious cycle, moreover, was becoming increasingly apparent by comparison to peers on financial metrics which are key for capital-intensive businesses: EBIT margin (a deficit of 1290 basis points to CNR in 2005 increased steadily over the CEO's tenure to a deficit of 1780 basis points in 2011), Return on Invested Capital (a deficit of 138 basis points in 2005 had become a deficit of 362 basis points by 2011), and the company generated no net cash over six years, after capital expenditures and pension funding in excess of expense.

The root cause, the dissidents argue, is a culture of little accountability—particularly for the CEO, and for the board which continued to accept the short-term challenges of operating the business—everything from floods and avalanches to shipping volumes recovering too fast—as a reasonable explanation for long-term failure to move the needle. The company's current "Multi-Year Plan" (MYP), the dissidents point out, is at least the 10th distinctive plan over the CEO's tenure, and many of its components are rebranded initiatives from previous plans. The net story over six years of the current CEO's tenure, they point out, is that operating results are in-line with the operating results from his first year in office: the company has made no progress.

While one dissident goal is to replace the CEO with Hunter Harrison, the former CNR CEO who created the precision railroading revolution, the dissidents also point out that the board, which long refused to hold the current CEO accountable for results, is the ultimate source of the company's cultural malaise, and any real reform of that culture requires reform of the board itself.

Management Response

The company asserts that its board does hold management accountable for results, in part through developing a robust Multi-Year Plan (MYP) whose aggressive OR target of 70-72% for 2014–an improvement of 9 to 11 percentage points better than 2011's OR of 81.3%—an independent consultant has affirmed is "within a reasonable range of achievement." The MYP itself focuses on growing revenues by creating "true strategic partnerships with key customers, market development, service excellent and inflation-plus pricing" even as the company works to improve productivity and contain cost, and expands it length of haul and network capacity. Though there has been significant change in the C-suite throughout the current CEO's tenure, the board argues it now has "the right team with the right plan," and has aligned the compensation of its executive team with success on the MYP.

That alignment of objectives and incentives, the company contends, is already paying off. In Q1 2012, the company reported diluted EPS of $0.82—up 310% over admittedly weather-weakened results in the same quarter of 2011, but also up 39% over Q1 results in 2010, when weather conditions for the railway were approximately similar. OR for the quarter came in at 80.1%—1,050 basis points better than the same quarter in 2010, but also 220 basis points better than Q1 2010. Operating managers and executives, moreover, have "line of sight" to further volume growth and improvements in productivity and cost savings, significantly increasing the board's confidence that the MYP itself is on track. On the strength of that line-of-sight evidence, the company has further refined its public targets to an OR of 68.5 to 70.5% for 2016.

Responding to the dissidents' criticism the company has languished under the current CEO's leadership, the board points out that the six years of his tenure have been marked by unprecedented adverse events—the sharp and deep global recession of 2008-2009, for example, which hit CP disproportionately hard given its mix of business, or the particularly brutal Canadian winter of 2010-2011, which disproportionately affected its ability to move freight. Even with those

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unforeseen but unavoidable challenges, the board points out, the company has managed to keep its operating expense unit cost comparable to CNR since 2006—if you adjust for the glaring difference in one legacy cost, corporate pensions.

The executive team has managed this in part by reining in discretionary capital spending—locomotive and freight car purchases, or network productivity enhancements to support the MYP, for example—necessary short-term measures which nonetheless adversely affected its progress on MYP objectives. The board's faith in the MYP itself, however, remains unshaken, and is now bolstered by rebounding volumes as external factor return to normal. Progress on the MYP has not stopped, moreover. In Q1 the company set records on key metrics of asset utilization which are predictive of MYP success: terminal dwell was down 27%, train speed up 27%, and car miles per day up 51%. Even equity analysts are recognizing the process, the board points out.

Revenue growth is an integral part of the MYP, and while the board estimates 80% of its routes have direct rail competition, the company has been de-risking the business through long-term contracts with major industry partners, improved service to help recover lost market share in grain and intermodal markets, and continued development of new markets in long-term partnership with key customers.

The dissident critique, the board concludes, is founded on a misreading of the facts—not surprising, given the intricacies of railway operations and the slipperiness of some analytic assumptions on which the dissidents have relied. Length of haul, for example, will result in lower unit operating costs if loading and unloading and other terminal expenses ("yard costs") are substantial. Among the 7 commodity groups, however, CP's business mix is more heavily weighted to things like coal, which have very little yard cost. Its routes also run through more difficult terrain than CNR—steeper grades and more curves, for example—which increases transport cost between terminals.

To address these criticisms, the board authorized the consulting firm Oliver Wyman not only to report back on the soundness of the company's own MYP, but also to evaluate the effect on the OR of these sorts of structural differences between the company and its closest peer, CNR. After a 4-month deep dive the consultant reported not only that the MYP targets were realistic, but that the dissidents' own proclaimed objective—and OR of 65% by 2015—was "neither realistic nor achievable". The structural differences between CNR and CP, the consultant determined, create a 670 basis point structural difference between the OR's the two companies can expect to achieve. This 670 basis points of deficit is increased slightly by 50 basis points due to CP's substantially worse legacy pension obligations, but also slightly offset by 160 basis points of advantage in its "market franchise", for a net structural discount of 560 basis points.

The strength of its MYP, the board argues, coupled with the evidence from recent quarters that the improvements are taking hold, all auger against swapping out the current board in favor of a dissident slate. As a gesture of its willingness to engage in constructive Board-level dialogue with shareholders, however, the board did offer a board seat to Pershing CEO Ackman and—despite his rejection of that offer—has included him as one of the management nominees it is recommending to shareholders in this election.

Analysis

When analyzing proxy contests, ISS focuses on two central questions:

1. Have the dissidents made a compelling case that change is warranted?
2. If so, are the dissident nominees more likely to drive that change?

Question 1. Is Change Warranted?

Total Shareholder Return

Over both the three- and five-year periods ending April 30, 2012, the company significantly underperformed most other Class 1 North American railways. Over the five-year period CP returned just 19.4%, while peers ranged from 56% to 117%. Over the three-year period, CP returned 90%— slightly above its closest peer Canadian National Railway (CNR), at 85%, but below other peers which ranged from 120% to as much as 415%.

The company's performance would likely have been considerably weaker had the dissidents not appeared. In the 5-year TSR analysis, for example, it is clear that the company was not on track to deliver even 19.4%: through Sept. 22, 2011, when Pershing began buying shares, it had lost 29.1%, while peers returned between 26.7% and 56.0%.

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Between Sept. 22, and Oct. 28, when Pershing filed its first 13D, prices increased by 32.9%. Between the 13D filing and the first reports Pershing would run a proxy contest, shares increased another 12.5%, for a compounded total of 49.5%.

In the subsequent period through April 30—which includes announcement of both Q4 2011 and Q1 2012 earnings—shares increased only another 10.7%, suggesting that while the market may have warmed to the news in those earnings releases, it had already put many of its eggs into the dissidents' basket.

Operating Performance

As much as the company may have underperformed its peers over sustained periods, the heart of the dissident argument is that the company has underperformed its potential. For a railway, particularly as the industry is changing all around it, the trend in Operating Ratio (OR)—total expenses divided by revenue, the industry's key measure of operating efficiency and fiscal health—relative to peers is a better indicator of its potential.

The trend in CP's OR is not flattering to either the incumbent board or the CEO.

In 2005, the baseline year just prior to the CEO's appointment, CP posted an OR of 77.7%—significantly worse than CNR, at 64.8%, but also significantly better than most of the company's US peers, which averaged 84.9%. Over each of the next six years, this 715 basis point advantage to US peers eroded. By 2008 it had become a net disadvantage of 317 basis points. By 2010 the disadvantage had nearly doubled, to 590 basis points. By 2011 it had tripled, to 1,040 basis points.

The board has argued that 2011 was an aberration due to an extremely difficult Canadian winter which disproportionately affected CP, particularly compared to US peers. It has also pointed out that the company's revenues were disproportionately affected by the global recession of 2008-9, given them greater exposure to commodities in its business mix. Intuitively, one knows that such factors must have some effect. What they do not explain, however, is the inexorable loss of what had been a sizeable margin advantage just six years earlier. If commodity cycles can work against you one year they must, one has to believe, work for you in other years, so that the dismal trend relative to peers does not extend unbroken. Strangely, this does not appear to have been the case. Even in the relatively stronger years of 2006 and 2007, when the company achieved its lowest ORs under the current CEO, the rate of year-over-year improvement was markedly lower than for the average US peer.

"Structural Reality"

CNR, which continues to have the lowest OR of any Class 1 North American railway, has begun to seem like a special case: there must be a mathematical limit to how low an OR can go, and CNR generally seems to define it. Yet even CNR improved its OR much more markedly than CP in 2006, and despite some fluctuation during the period of the global recession, still managed to lower its OR meaningfully by 2010 and 2011 compared to the baseline year of 2005.

It may not be surprising, then, that a board facing this set of facts would commission a consultant to quantify just how much of the deficit to CN, as the industry leader and closest peer, was a "structural reality." The answer turns out to be 670 basis points. An additional 50 basis points accrue from adverse "pension and labor," offset by 160 basis points of comparative advantage for CP's stronger "market franchise." The net effect, once the dust settles, is 560 basis points of OR reduction which CNR might achieve, but CP could not.

This is a stunning admission, and not in the way the board must have intended.

If by management's own reckoning the things it cannot control explain 670 basis points of margin deficit, the remainder, by definition, must be the performance of the management team itself. Since no new mountain ranges have added to the "structural" deficit, any incremental OR disparity in comparison to CP must, one presumes, be attributable to management action or inaction.

At the close of 2005, the company's OR stood at 77.7%, 1,294 basis points worse than CNR. Assuming, for the sake of argument, that 670 basis points is indeed the right measurement of things management cannot control, it would appear that management's own contribution was to <u>increase</u> the margin deficit by another 624 basis points in that year. A year later, after the CEO's first year in office, the total deficit had grown by another 164 basis points.

One could argue that the OR in any single year is affected by other factors, such as weather, not considered by the consultant's report. One cannot ignore, however, that the deficit to CNR was larger, in all but one year of the CEO's tenure,

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than the deficit he inherited. CP's average OR of 78.6% over his entire tenure, moreover, was both higher than the OR he inherited, and increasingly far behind the best-in-class OR of 64.2% which CNR averaged over the same period. The portion of the OR deficit attributable to managerial effectiveness averaged 773 basis points over his tenure, significantly higher than the "structural" deficit on which the board has fixed its focus.

Managerial effectiveness

This management-driven OR deficit appears to be the result of two things: the CP team reaching détente with its OR, and the CNR management team continuing to attack its OR. Over the CEO's tenure, CP added 362 basis points to its OR; CNR's management team took 127 basis points out of its OR.

Even measuring only to the end of 2010, to control for the weather in 2011, the story is less dramatic but still follows the same unfortunate plotline. Over that period CP took a total of 11 basis points out of its OR—not quite 2 basis points per year, on average. CNR took 121 basis points out of its OR.

But to object about the weather in 2011 is, once again, to ignore the central fact that, over the CEO's entire tenure, this performance cannot be explained by a spell of bad weather: even in times of relatively good weather, the company does not appear to have made up the ground it was losing. CP is not, moreover, the only North American railroad which faces weather and other "unforeseeable" short-term challenges. CNR has significant exposure to the Canadian winters, even if not identical exposure, and the company's US peers have significant exposure to other weather-driven misfortunes, such as flooding.

More importantly, the short term eventually gives way to the long-term. The point of hiring a management team is the expectation they will manage away short-term constraints over the long-term. The Class 1 US railroad peers appear to have spent the last six years demonstrating just how a management team can meaningfully address the short-term constraints embedded in a high OR.

Three of the four US railways, each of which started the period with an OR above 80%, improved by more than 1,000 basis points from 2006-2011. One could argue they were simply taking low-hanging fruit, including pricing, which was unavailable to CP—except that the fourth, already significantly ahead of these other peers and CP, also improved its OR by another 400 basis points. Of the 1,754 basis points by which CP's OR degraded versus the US peer average, 1,393 basis points were due to structural changes implemented by those management teams which drove improvements in their ORs across both weather and business cycles. Even just looking at performance through 2010, when CP had delivered just 11 basis points of OR improvement, the average US peer had improved by 1,315 basis points.

Summary: Is Change Necessary?

The issue for shareholders—who are ultimately invested for return—is exactly this issue that only the dissidents have spoken to: the performance of their investment over time. An investment which, unlike every one of its peers, had been losing value until an activist shareholder stepped in is unlikely to be explained away with a welter of metrics demonstrating that return isn't all that central. For all the metrics and charts and tables of operating statistics which have been marshaled in this contest, the metrics which matter most to shareholders are returns over sustained periods, and the predictability—here, evidenced by the trend in Operating Ratio—of future return. Given that the first of these was clearly going in the wrong direction for a long time before the dissidents arrived, and the board's defense of the second amounts to sleight-of-hand, it seems clear that some change at the board level is needed.

But the dissidents have raised a larger question of culture—which is not measured directly by, but is embedded within, both TSR and the income statement. This is worth exploring further, as it appears to speak to the root cause of the problem.

One helpful signal that a corporate culture may lack accountability might be the impulse, when faced with a potential proxy contest over poor performance, to hire a consultant—five senior partners, shareholders have been soberly informed, working more than 5,000 hours over 4 months—to measure what is impossible to achieve, then use those results to explain why management and the board cannot be held accountable for underperformance.

The most compelling conclusion one can draw from the episode of the consulting study, in fact, is exactly the point the dissidents have made from the start. "Structural" disadvantages are not the company's biggest challenge—but the overpowering need to explain that things are simply beyond your control just might be. If the point of the study was to

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clarify for management exactly what was not expected, a useful takeaway might be that it's not always worth clarifying how low the expectations can be set.

What is still missing from the board's discussion about operating constraints and Multi-Year Plans, moreover, is a real sense of what is required to execute on a true, robust strategy—perhaps because playing catch-up is not in itself a strategy. This comes through most powerfully not in the discussion of the MYP itself, interestingly, but in flurry of personnel changes in the C-suite during the CEO's tenure. In those six years the company has changed COO's five times, and swapped out CFO's three times. Once is understandable: people move on for any number of reasons. Twice is unfortunate but still perhaps understandable: sometimes things aren't what they seemed, and you have to cut your losses. Six times is akin to playing Whack-A-Mole in the C-suite, and may say more about the abilities of the CEO and board than about any individual candidate. How, one might ask, is it possible to plan for the long term, much less execute on those plans, when succession planning in the executive suite looks more like crisis management?

This proxy contest is ultimately less about running a railroad than it is about credibility and expectations. The central railroading question isn't even whether an OR of 65 is possible, as the dissidents argue, by 2015: it is why all the current sense of urgency about reaching an OR of 70-72%, safely beyond the range of the impossible "structural" constraints, wasn't manifested by this same board half a decade ago. If the answer to that question is that first macroeconomic, then weather-related, crises intervened, it quickly gives way to a more urgent question of why anyone would believe there will be no more macroeconomic or weather-related crises over the next three to five years, when the same board and CEO are presumably going to get around to delivering these operating improvements.

Question 2: Which Nominees?

Nominees

The dissidents have nominated 7 director candidates:

William Ackman (45) is CEO of Pershing Square Capital Management, L.P., an investment adviser with $11 billion of assets under management, which he founded in 2003. He serves on the boards of three other public companies.

Gary Coulter (66) is CEO of CRS, a restructuring and strategy management consulting firm, and was previously Vice Chair of KPMG Canada. He serves on the boards of three other public companies.

Paul Haggis (60) is Chairman of Alberta Enterprise Corp, was previously CEO of both the Ontario Municipal Employees Retirement Board (OMERS) and Alberta Treasury Branches, and COO of Metlife in Canada prior to that. He serves on the boards of three other public companies.

Paul Hilal (45) is a partner at Pershing Square and the firm's lead on the CP investment. He has previously served, but does not presently serve, on other public company boards.

Rebecca MacDonald (58) is Executive Chairman of Just Energy, a $1.8 billion publicly-traded company which is the second successful energy marketing company she has founded. She currently serves on the board of one public company, Just Energy.

Tony Melman (64) is currently Chairman and CEO of Nevele, a provider of strategic business and financial advice. He has previously served, but does not presently serve, on other public company boards; he is, however, a director of the Ontario Lottery and Gaming Corporation.

Stephen Tobias (67) was Vice Chairman and COO of Norfolk Southern from 1998 to 2009, and has 40 years experience in the railway industry. He is a director of one other public company.

Ackman, to whom the company had offered one board seat, is a nominee on both slates. In addition, the company has nominated 15 incumbent directors:

John Cleghorn (70) joined the CP board in 2001, and currently serves as Chairman. He has more than 35 years of financial sector experience, 6 years as Chairman and CEO of the Royal Bank of Canada, through his retirement in July 2001. He currently serves on two other public company boards, including the board of Canadian Pacific Railway Corp. (CPRC).

Tim Faithfull (70) joined the CP board in 2003, and currently chairs the Safety, Operations, and Environment (SOE) Committee. Over a 36-year career with Royal Dutch/Shell plc, he filled diverse international executive, operational and commercial roles, retiring as President and CEO of Shell Canada Limited in 2003. He currently serves on four other

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public company boards including CPRC.

Richard George (61) joined the CP board in 2011. He has served as CEO of Suncor Energy, Canada's largest integrated energy company, since 1991, and was named "Outstanding CEO of the Year" in 1999 after leading the turnaround of that business, and Canadian Energy Person of the Year in 2011 by the Energy Council of Canada. He currently serves on the boards of two other public companies, including Suncor.

Fred Green (55) joined the CP board when he was named CEO in 2006. He has held various positions at the company in operations, sales and marketing, and yield. He also serves on the board of CPRC.

Ed Harris (62) joined the CP board in 2011. He has worked in railway operations for 44 years, including senior operating positions with Illinois Central, Canadian National, and, following his retirement from CN, as an independent rail operations consultant, before becoming COO of CP for approximately 9 months between 2010 to 2011. He is also a director of CPRC.

Krystyna Hoeg (62) joined the CP board in 2007. She served as President and CEO of Corby Distilleries Limited, from October 1996 to February 2007, and previously held a number of senior financial positions at other firms within that industry. She currently serves on four other public company boards, including CPRC.

Tony Ingram (65) joined the CP board in 2011. He has worked in the railway industry since 1970, initially in engineering and labor relations before moving to train operations, eventually becoming COO of CSX Transportation Inc. from 2004—2009. He is also a director of CPRC.

Richard Kelly (68) joined the CP board in 2008. He was Chairman and CEO of Xcel Energy Inc., from 2005 until his retirement in 2011; he had previously served as CFO of that firm and of New Centuries Energy. He is also a director of CPRC.

John Manley (62) joined the CP board in 2006. He was the Member of Parliament for Ottawa South from November 1988 to June 2004, during which period he held various positions in the Canadian Federal Government including Deputy Prime Minister from January 2002 to December 2003, Minister of Finance from June 2002 to December 2003, Minister of Foreign Affairs from October 2000 to January 2002 and Minister of Industry prior thereto. He has been President and CEO of the Canadian Council of Chief Executives since 2010, and was counsel at the law firm of McCarthy Tétrault LLP prior to that. He serves on three other public company boards, including CPRC.

Linda Morgan (59) joined the CP board in 2005. She was previously Chairman of the United States Surface Transportation Board, the primary regulatory rail authority in the United States, and its predecessor the Interstate Commerce Commission, from March 1995 to December 2002. Prior to joining the Interstate Commerce Commission, she served as General Counsel to the Senate Committee on Commerce, Science and Transportation. She is currently a Partner at Nossaman LLP. She is also a director of CPRC.

Madeline Paquin (49) joined the CP board in 2001. She has been CEO of Logistec Corporation, an international cargo-handling company, since January 1996. She is also a director or member of a number of maritime advisory and transportation associations. From 2003 to 2006 she was among the winners of Canada's Most Powerful Women: Top 100 award from WXN and has since been inducted to its Hall of Fame. In 2011, she was named Business Woman of the Year by the Chamber of Commerce and Industry of Trois-Rivieres. She serves on two other public company boards: CPRC and Logistec.

Michael Phelps (64) joined the CP board in 2001. After an 18 month stint as CFO he served as CEO of Westcoast Energy Inc. from 1988 until the company merged with Duke Energy Corp. in 2002. He is currently Chairman of Dornoch Capital Inc., a private investment company, and serves on four other public company boards, including CPRC.

Roger Phillips (72) joined the CP board in 2001. He was CEO of IPSCO Inc., a steel manufacturing company, from 1982 until his retirement in 2001; he had previously held senior management positions over a 21-year career with the Alcan group of companies. He currently serves on two other public company boards, including CPRC.

David Raisbeck (62) joined the CP board in 2009. He was Vice-Chairman of Cargill Inc. from 1999 to 2009, where he had held a number of other senior management positions since joining the firm in 1971. He serves on three other public company boards, including CPRC.

Hartley Richardson (57) joined the CP board in 2006. He has been CEO of James Richardson & Sons, Ltd., a privately-owned corporation involved in the international grain trade, real estate, oil and gas development, financial services, and

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private equity investments, since 1993. He serves on three other public company boards, including CPRC.

Winnowing

As each side has provided a universal ballot, shareholders are asked to vote for as many as 16 out of 22 total nominees.

Shareholders who do not believe the dissident has made a compelling case for change have a full slate of 16 candidates identified for them by the management circular. Unlike many proxy contests, however, in which the dissident shareholder identifies both only the new nominees it would like shareholders to elect to the board and the incumbents it would like those nominees to replace, Pershing Square has made no recommendation with regard to any of the incumbent directors. Accordingly, shareholders who believe the dissidents have made a compelling case for change now have the opportunity to select what they believe will be an optimal board from among all 22 candidates.

ISS is generally reluctant to recommend for multiple nominees from the same investment fund, out of the belief that director independence matters and that the power of ideas, not the force of numbers, should win out in the boardroom. In nominating Ackman to its slate, however, the company—unless it was being disingenuous in its offer—has effectively signaled that Pershing Square's CEO is a qualified director candidate who would add value. Dissident nominee Hilal is thus the only disputed Pershing Square executive seeking a board seat, and should be considered on his own merits as a candidate, not as a second to another disputed candidate. Clearly, even the board believes Hilal brings something different to the table than Ackman.

Because we believe the dissidents have demonstrated a compelling case for change, we have evaluated the 22 nominees according the experience and perspective the company will require from its board to effect that change:

- Board leadership and accountability for results;
- Turnaround experience, including strategic evaluation and planning;
- Deep knowledge of the industry, including railway experience;
- Regulatory and/or government experience; and
- The proven ability to get things done, a trait generally correlated with successful senior executive operating and finance experience.

It should be clear, however, that stronger candidates will have experience or perspective across several of these categories, of course: a successful public company CEO or CFO will necessarily have some strategic planning experience, and every public company director should have a deep sense of accountability for results.

Board leadership and accountability for results

Shareholders may reasonably expect that the board's incumbent leadership—Cleghorn, as a long-serving CP director and current chairman, and Green, whose tenure as CEO now extends for more than half a decade—would have taken responsibility for steering the company closer to its true potential. What shareholders appear to have witnessed over these directors' tenure, as a close examination of the evidence in this proxy contest makes plain, is an enduring failure of board leadership, and a bewildering lack of accountability for results. This has nothing to do with these directors' success in their prior careers: the point of bringing a successful executive onto a board, much less into a board leadership position, is to spur new and further success through board service. Over what is now a very large number of years both Cleghorn and Green have failed to deliver on that expectation.

Faithfull, who also had significant career success as an executive prior to joining the CP board, has similarly failed to provide strong leadership despite chairing the Safety, Operations, and Environment (SOE) committee which has the most direct oversight of the exact areas in which the company has continually failed to recognize, much less achieve, its potential. Particularly stark is the SOE's decision to commission a consulting study to pinpoint just how much management could not possibly improve the business—then failing to note that, perhaps inadvertently, the same study had also quantified what turned out to be the significantly larger problem: management's failure to manage effectively the remaining aspects of the business which are under its control. If the committee's central focus was the operations, one has to ask, how did it miss the enormous and still-accumulating evidence that the company's operations were falling significantly behind every one of its North American Class 1 peers, and shareholder value was suffering as a result?

The fact that Ackman was endorsed by both slates may signal that there is little doubt about his ability to deliver value as a director. More direct and compelling evidence, however, might be the effects of his board service on some of his fund's

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other significant portfolio companies. At JC Penney, to draw just one obvious parallel, the board has undertaken significant strategic and managerial changes after Ackman, who had a distinct view on those matters, joined the board. Since that firm first announced the change in strategy in January 2011—in part because it has clearly executed on what it promised to investors—its shares (which had already doubled since Ackman's investment was announced) have appreciated at approximately twice the rate of the broader US market. Given Ackman's role, moreover, it matters less that the company is a retailer rather than a railroad, and far more that since Ackman took a board seat the company has acknowledged its issues, then developed, explained, and consistently executed on a strategic plan to recover its potential. It is also significant that at JC Penney when Ackman took a board seat, like CP now, his fund had a significant investment in the stock and a correspondingly significant interest in ensuring the turnaround took root.

Dissident nominees MacDonald and Haggis, as well, have demonstrated a keen sense of accountability in their executive and board experience. After building and running Just Energy for a number of years, MacDonald moved to an Executive Chairman role in 2005 and promoted her long-time number 2, himself a founding partner, to the CEO role. Three years later, when her co-founder demonstrated he was unable to meet the sales targets he himself set, she replaced him, taking on part of the CEO's responsibilities on an interim basis. Significantly, the move was not spurred by a dire public event such as missing quarterly guidance—but by the board's close monitoring, under her leadership, of key leading metrics, and its willingness to address a difficult, clearly uncomfortable issue before it devolved into an adverse event for shareholders. Haggis, similarly, has several times in his career—most notably at Alberta Treasury Branches, and then again at OMERS—taken on difficult issues as an executive and director. One significant difference, however, is that he has shown a willingness to take up the challenge, as both of these nominees would now do if elected at CP, long after the issues had boiled over into adverse events. At OMERS, to cite one example, he began his tenure as CEO by driving a re-evaluation of its real estate, infrastructure, and private equity assets, resulting in a $600 million write-down as these assets were marked to market. The write-down itself reflected prior performance—market values falling away—but the willingness to confront the obvious, despite the pain, so that the organization could move forward, reflects the kind of leadership the CP board will need in addressing the challenges ahead.

Turnaround experience; strategic evaluation and planning

In addition to Haggis, the dissidents have nominated two candidates with direct experience advising firms on strategic issues: Coulter, whose current firm focuses on restructuring and strategy, and Melman, whose firm provides strategic and financial advice. In both cases there appears to be as well a fluency in the language of business. Coulter spent 34 years advising companies with KPMG Canada, including 27 as a partner and a decade as Vice Chairman of the firm's Financial Advisory Services business; he has also served on audit and governance committees of a number of large public companies. Melman was an executive with a publicly-traded private equity firm, Onex Corp., for more than two decades prior to taking his current role at Nevele.

Like Haggis, management nominee George has led a significant turnaround as an operating executive, for which he was recognized as "Outstanding CEO of the Year" in 1999. As importantly, he has the experience of remaining with the firm after the turnaround itself, helping to ensure it stayed on track and became part of the culture itself. Raisbeck—another more-recent addition to the CP board—also has senior executive experience running Human Resources, a key consideration in a turnaround, for another large company, Cargill Inc.

Industry knowledge and railroad experience

Of the three nominees with industry operating experience, dissident nominee Tobias stands out both for the depth of his senior-level experience—more than a decade as COO and Vice Chair of Norfolk Southern, during a period when that company bought and integrated Conrail—as well as for the fact that he supervised and presumably helped develop one of the management nominees, Ingram, before Ingram went on to become COO of CSX from 2004-2009. Management nominee Harris, too, has served as COO of a major North American railway—CNR, under Hunter Harrison.

On the surface of things there is little reason to doubt any of these three former railway COO's would, individually, be unable to add value to the CP board. The question really arises, however, whether adding a second, and particularly a third, continues to add additional value to the board. In Harris' case, we also note, he worked for nearly a year as COO of CP itself, then worked as a consultant to the company, before being elevated to the board—to oversee the same CEO to whom he'd just been reporting. This is a strange governance play—and Harris's repeated public pronouncements throughout this contest that Green is the right CEO for CP, despite all the evidence to the contrary, raises questions about his commitment to facing hard truths in the service of all shareholders. The point of bringing railway executives onto the board, after all, is

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specifically to assess whether and where management has been failing—not to shill for them despite manifest failure.

Neither Hilal nor management nominee Paquin have railway operating experience. Then again, this is not a contest driven by the details of railway operations—it is a contest driven by the inability of a board to set reasonable expectations of operating executives on behalf of shareholders, and then to hold management accountable for delivering on those expectations. In his role as Pershing's lead partner on understanding the potential of an investment in CP—let alone laying out that very complicated case to shareholders in this proxy contest—Hilal has demonstrated a deep understanding of what is necessary to deliver the promise of the company, and how to measure progress toward that goal. Paquin, with executive experience and contacts in the transportation industry more generally, should also be able to add broader context to strategic discussions. As a director since 2001, though, one would have expected her to leverage this ability long ago, before things reached the bad eminence of a shareholder proxy contest to replace the CEO, Chairman, and five other directors.

Regulatory/government experience

The value of regulatory and government experience is not perhaps as immediate as others of the categories outlined in this analysis of board needs. Railways are highly regulated entities, however; deep regulatory/government experience is likely a significant long-term board need, in ways that are possibly more visible inside than outside the boardroom. Management nominee Morgan, with extensive experience in US regulatory affairs (including leading the principal US regulator for railways), has clearly relevant experience for both the near and long-term. Management nominee Manley, as a former minister of the Canadian federal government, also brings senior government experience and contacts within the company's core market. Dissident nominee Haggis, too, has developed significant government experience and network in western Canada, on a level different from that of the federal government.

Successful operating / finance executive experience

Many of the director candidates already discussed—especially dissident nominee MacDonald, who has created large, successful businesses from scratch, and dissident nominee Haggis and management nominee George, who have each led successful turnarounds at large businesses—help meet the need for directors with successful operating and finance executive experience. Management nominees Hoeg and Kelly, who are relatively newer additions to the board, each served as a CFO before taking a CEO role, and stand out as additional strength. Management nominees Richardson and Raisbeck have significant experience, though it was at privately-held companies without the additional layer of public shareholders. There is no reason to believe the successful operating experience itself, however, would be less useful on the board of a large public company.

The management nominees Phillips and Phelps, by contrast, ended their executive careers a decade ago, and their board tenure—each joined in 2001—does not suggest they will continue to add incremental value beyond what the other candidates with operating executive experience bring. Phillips, in addition, is bumping up against the board's mandatory retirement age.

Other considerations

There is one potential issue if CEO Green is voted off the board: it is unusual, and over a long term may be unwise, to not have a seat reserved for the CEO at so large a public company. In the short term, we believe Green has not served shareholders well enough as a director to merit support in this proxy contest. Over the longer term, we would expect to see the company appoint its anointed CEO to the board.

But if 16 directors, which is no one's definition of "nimble," may be more board than this company needs, 17 cannot be the right answer. Before the incumbent board began bulking up in response to Pershing, the total was 13 directors including a CEO—though even that number may not be the right size for effectively addressing what is in front of it.

Even as they are being asked by the universal ballot to optimize the board, however, shareholders cannot address this issue directly: the top 16 vote-getters will be seated, regardless of whether individual shareholders vote for fewer than 16 as a signal the board should be right-sized. Given this dilemma, we believe it is more prudent for shareholders to elect the 16 candidates they believe are most compelling, and rely on those 16 to determine if and how the board should be resized after that.

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Conclusion

Because the dissidents have demonstrated a compelling case that poor board oversight has allowed the company's performance to drift further and further below both its peers and its potential over at least half a decade, it seems clear that change on the board is needed.

After assessing the challenges the board now faces in addressing these issues –and recognizing that many nominees will add value across several of the following categories—we recommend shareholders vote FOR the following 7 dissident and 9 management nominees:

- Ackman, MacDonald, and Haggis to restore board leadership and imbue a sense of accountability to shareholders;
- Coulter, Melman, and George for their strategic experience, particularly as it applies to corporate turnarounds;
- Tobias and Ingram for their railway operating experience;
- Hilal and Paquin for their knowledge of the industry and its opportunities;
- Morgan and Manley for their regulatory and government experience and contacts; and
- Hoeg, Kelly, Richardson and Raisbeck for their successful executive experience in operating and finance roles.

Because there are more nominees on each ballot than the number of available seats—and also, for certain directors, out of specific concerns about their performance on this board—we recommend shareholders DO NOT VOTE for the following six management nominees

- Green and Cleghorn and Faithfull, who have failed to provide effective leadership and accountability to shareholders in their respective roles as CEO, board Chairman, and chairman of the Safety, Operations, and Environment committee;
- Harris, for the strange and ultimately unnecessary governance issue raised by taking a board seat to "oversee" the performance of the CEO he had just recently reported to;
- Phillips, who has reached the board's mandatory retirement age; and
- Phelps, whose long tenure has not helped shareholders avoid the long decline relative to peers and the company's potential.

Equity Ownership Profile

Type	Votes per share	Issued
Common Equity	1.00	170,856,685

Ownership - Common Equity	Number of Shares	% of Class
Pershing Square	24,159,888	14.2

Additional Information

Meeting Location	Fairmont Palliser Hotel, 133 - 9th Avenue S.W., Calgary, Alberta
Meeting Time	08:00
Shareholder Proposal Deadline	Dec. 21, 2012
Security IDs	13645T100(CUSIP)

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