

# PUBLIC MARKETS

As a long-term investor, PSP Investments believes in strong governance oversight of its investments. We use our ownership positions to promote good corporate governance practices by exercising our proxy voting rights. We also actively engage with companies, individually, through service providers and via collaborative initiatives with other like-minded investors.

Before allocating funds to an external manager, we perform due diligence to confirm that the manager's policies and procedures are aligned with our Responsible Investment Policy. We also ensure the manager's investment processes are capable of identifying ESG factors and responding to ESG risks.

## EXERCISING OUR PROXY VOTING RIGHTS

Our [Proxy Voting Guidelines](#) address issues of corporate governance, on which we may vote from time to time, as well as the principles on which we rely when voting. We give due consideration to corporate governance principles when assessing the merits of an issue, and exercise our voting rights, with a view to maximizing the value of our shareholdings.

With regards to our active management of proxy voting:

- › We review proxy circulars and research reports from service providers when voting on equities held in accounts managed internally, and in segregated accounts managed externally.
- › We review and amend our Proxy Voting Guidelines biennially, primarily to further articulate our expectations of issuers in certain governance areas.

Most proposals made at shareholders' meetings are submitted by company management and relate to the election of directors and the appointment of auditors, as well as other matters that arise in the normal course of business. In some circumstances, under applicable laws or exchange rules, special meetings of shareholders may be called to approve transactions, such as mergers and acquisitions, security-based compensation arrangements and dilutive transactions.

PSP Investments strives to vote at all shareholders' meetings organized by companies in which we invest. However, we often choose not to vote in certain jurisdictions where share-blocking restrictions apply. Share-blocking is the practice whereby shares, when voted, can be temporarily restricted from trading during the time leading up to and, sometimes, immediately following the date of the shareholders' meeting. We do not support share-blocking restrictions because they limit portfolio management capabilities.

### FISCAL YEAR 2017 PROXY VOTING ACTIVITIES

Voting rights exercised	Exercised at 3,871 meetings, for a total of 41,912 resolutions
Share-blocking restrictions	Unable to exercise voting rights at less than 1% of meetings

**In fiscal year 2017, we voted against or abstained to vote on approximately 9% of the 40,625 resolutions proposed by management.**

**This table presents a breakdown of these votes on a per issue basis.**

#### VOTES AGAINST MANAGEMENT PER ISSUE (FY 2017)



## ADVOCATING FOR EFFECTIVE BOARDS

As a long-term institutional investor in the global equity markets, we believe that sound corporate governance practices and responsible corporate behavior contribute to the long-term financial performance of public companies in which we invest and are important to well-functioning securities markets.

### Independence

PSP Investments believes that strong independent boards are best positioned to successfully direct a company and oversee management with a view to creating long-term shareholder value.

**During fiscal year 2017, we withheld or voted against selected board nominees due to lack of independence, non-separation of the roles of Chair and CEO, poor attendance records and/or time-commitment issues.**

### Diversity

PSP Investments believes that strong boards and management teams — composed of qualified individuals with a diverse range of views, backgrounds and experiences — enhance decision making. We encourage issuers to promote diversity at all levels of their respective organizations.

Where diversity is lacking, we expect issuers to take the necessary steps to become more inclusive, especially at the board and management levels. This includes adopting and disclosing policies and targeted objectives, and improving reporting.

### Effectiveness and integrity

On an annual basis, when proposing nominees for election, boards and nomination committees should consider board renewal in light of both director tenure and performance. In exceptional situations, where there are issues relating to corporate governance coupled with a lack of board renewal, PSP Investments may vote against, or withhold support from, the chair of the nominating committee.

We maintain that shareholders should have an opportunity to vote for or against each director annually on an individual basis, rather than as a slate or in a staggered fashion. We also support the adoption of a majority vote standard for the election of directors.

*“The Responsible Investment group plays a key role in our efforts to improve corporate governance policies and practices at the companies in which we invest. The group promotes transparent decision-making processes at the board and management levels, and advocates for the full disclosure of material information. This is fundamental to the efficient operation of capital markets.”*

— Jérôme Bichut, Managing Director, Public Equity Portfolio

## COMPENSATION

PSP Investments believes that executive compensation should be appropriately structured to enhance shareholder value while rewarding performance which meets or exceeds stated objectives.

For non-executive directors, compensation should be set at a level that is financially worthwhile, but not so high that they become beholden to an issuer or compromise their independence. For management, compensation should be sufficient to attract, motivate and retain highly-qualified executives and be linked to risk-adjusted performance.

We support shareholders' resolutions that call for annual non-binding ratification of executive compensation policies. We assess pay practices on a case-by-case basis. We take into account pay-for-performance alignment. CEO compensation must be consistent with that of other senior executives and there must be meaningful performance targets for long-term incentive compensation. We encourage issuers to adopt recoupment (clawback) policies.

**In fiscal year 2017, we voted against several compensation-related proposals that were misaligned with performance or failed to adequately disclose performance conditions. We also voted against several overgenerous or "single-trigger" severance compensation arrangements (golden parachutes) for executives that would have resulted from a proposed merger or acquisition.**

## CAPITAL STRUCTURE

PSP Investments generally supports changes to a company's capital structure, provided there are sound business reasons for the proposed changes.

**We voted against certain changes to capital structures in fiscal year 2017 because of dilution issues that were not justified by business considerations.**

## PROXY ACCESS

PSP Investments believes that shareholders should have a meaningful say in the director nomination process. Current best practices in Canada suggest that nominees should be chosen by an independent nominating committee of the board. The nominee slate, however, can potentially reflect the board's or the chief executive officer's network of relationships and perspectives. In our view, board composition in Canada would benefit from shareholder input into the nomination process. Such input is essential to shareholder democracy.

Current proxy access mechanisms do not always effectively provide shareholder nominees with prominence in the circular that is likely to give them an effective proxy access platform. We support an enhanced proxy access that will increase shareholder involvement in the director nomination process.

## AUDITORS' IRREGULARITIES

PSP Investments supports the election of auditors if they meet generally accepted independence standards and have discharged their responsibilities with diligence and integrity.

**On a limited number of occasions during fiscal year 2017, we voted against auditors who, in our opinion, did not meet the standards mentioned above.**

## AMENDMENTS TO ARTICLES OF INCORPORATION

PSP Investments is sometimes asked to consider and vote on resolutions regarding amendments to the articles of a company. Examples include those which would limit the right to call a special meeting or would change the jurisdiction of a company's incorporation.

We review resolutions proposing amendments to articles changing a company's governance structure on a case-by-case basis. We generally vote against amendments that reduce shareholders' rights.

## ANTI-TAKEOVER PROTECTION AND MERGERS

PSP Investments evaluates takeover-protection policies and proposals as well as shareholder rights plans on a case-by-case basis.

**During fiscal year 2017, we voted against takeover proposals, policies and shareholder rights plans that were not structured to maximize shareholder value or compromised shareholders' rights.**

## SHAREHOLDER PROPOSALS

Shareholder-initiated proxy proposals can be useful and relevant when addressing concerns and effecting change at companies that underperform or have poor environmental, social and governance practices. PSP Investments reviews all shareholder proposals on a case-by-case basis. We generally support shareholder proposals that increase board accountability to shareholders and serve the company's financial interests, if they do not put excessive constraints on the company, its board or its management.

In fiscal year 2017, PSP Investments voted on 1,287 shareholder proposals, and supported 43% of them.

### EXAMPLES OF SHAREHOLDER PROPOSALS SUPPORTED

SHAREHOLDER PROPOSAL THEME	NUMBER OF PROPOSALS SUPPORTED	RATIONALE FOR SUPPORTING SHAREHOLDER PROPOSALS
Proxy access	58	We believe that shareholders should have a meaningful say in the nomination process of directors.
Compensation-related proposals	30	We support proposals that increase executive compensation disclosure and further align the interests of executives with those of shareholders.
Report on sustainability and other environmental matters	49	We support proposals that seek to increase the level of board accountability to shareholders on sustainability and environmental matters.
Political contribution and lobbying reports	43	We encourage the full and transparent disclosure of company practices regarding political contributions and lobbying. On occasion, when no disclosure is available, we will support shareholder proposals requesting disclosure.
Independent Board Chair and separation of Chair and CEO	24	We believe that a Board Chair should be an independent director.

# ENGAGING WITH PUBLIC COMPANIES

We actively engage in direct dialogue with public companies to improve their ESG practices in respect of a wide range of issues, such as pollution and waste management, health and safety, supply chain management, board independence and executive compensation. We engage with companies in our public equity portfolio to encourage sustainable corporate conduct aimed at enhancing long-term financial performance.

Public companies are selected for engagement based on a process that takes into account such factors as ability to create shareholder value, prospects for successful engagement and relevance of ESG issues. The intensity of our involvement evolves over time. Some engagements entail one or two meetings over several months; others are more complex and warrant multiple meetings with board members and senior management over several years. We establish our engagement objectives based on issues for which we believe behavioural changes are warranted. Often, multiple ESG issues need to be addressed within a given company. Each of them may require varying approaches to – and levels of – engagement, as well as different contact points.

For extensive engagements, a five-step milestone approach is used to guide the engagement process and assess its success.

## Five-step engagement process

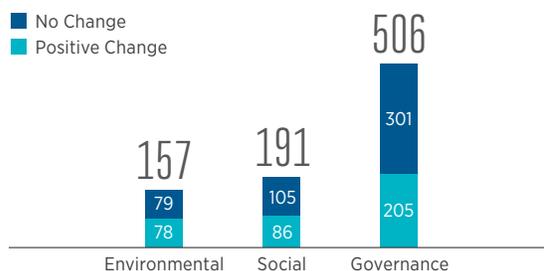


*“Our Responsible Investment group takes a proactive role when engaging with companies and peer organizations on environmental, social and governance issues. The group favours dialogue and collaboration, and its efforts produce tangible results. For example, in fiscal year 2017, its interventions with one board allowed a company to achieve its strategic objectives and deliver a transaction that proved beneficial to shareholder value.”*

— Anik Lanthier, Senior Vice President, Public Markets and Absolute Return Strategies

In fiscal year 2017, PSP Investments made progress in delivering engagement objectives across various themes and regions. The progress it has made in the achievement of new milestones for each objective is shown in the following graph.

ENGAGEMENT OBJECTIVES ANNUAL PROGRESS (FY 2017)



COMPANIES ENGAGED WITH BY COUNTRY OR REGION (FY 2017)



In fiscal year 2017, with the assistance of a service provider, PSP Investments engaged directly with 477 publicly listed companies whose securities it holds. These engagements were undertaken globally.

Our engagements cover a range of ESG issues. A breakdown of our engagement activities by issue is shown below, together with examples for each category.

ENGAGEMENTS BY THEME (FY 2017)



THEME	EXAMPLES OF ISSUES DISCUSSED
Governance	Director independence, majority voting, separation of Board Chair and CEO roles, succession planning, committee structures, performance-linked compensation, disclosure, and risk management, including bribery and corruption risk.
Social	Labour and community relations, health and safety, human rights and cyber security.
Environment	Climate change, water stress, biodiversity, forestry and land use, pollution and waste management.

## ENGAGEMENT IN ACTION

PSP Investments engages in direct dialogue with companies to discuss concerns on ESG risks. These are examples of engagements we have undertaken with the view of enhancing long term financial performance.

Global internet media company	
<b>ENGAGEMENT OBJECTIVE</b> Ensure better alignment of Board composition with the company's strategy.	<b>BACKGROUND</b> The company was contemplating a significant shift in its business and had undertaken a review of strategic alternatives. There was a lack of Board consensus on strategic orientation and, due to the disagreement, two Board members resigned. The dissent raised questions about the Board's ability to guide the company in its strategic realignment.
<b>ACHIEVEMENTS</b> <ul style="list-style-type: none"><li>› During discussions with the company, it acknowledged the importance of appointing new Board members who have an understanding of the company's strategic direction. Board composition criteria were adjusted to include individuals with extensive restructuring experience and the skill set to evaluate new opportunities, including restructuring opportunities. The Board now works in a more consensual manner and has the capacity to effectively evaluate proposals to create shareholder value.</li></ul>	

Asian semiconductor manufacturer	
<b>ENGAGEMENT OBJECTIVE</b> Improve health and safety practices.	<b>BACKGROUND</b> We initiated our engagement with the company in 2014, following media reports of health and safety related incidents, including a gas leak incident in 2015.
<b>ACHIEVEMENTS</b> <ul style="list-style-type: none"><li>› PSP Investments urged the company to consider implementing a comprehensive strategy to identify and address health and safety risks, including provisions for training and support for staff and contractors.</li><li>› After acknowledging gaps in its environmental, health and safety framework, company management created an Environmental, Health and Safety Office reporting to the CEO. Other improvements included additional supervision for high-risk tasks, risk-focused staff training for onsite work, the extension of training and medical coverage to contractors, and the creation of a system to document the health and safety record of contractors.</li><li>› In response to our request to improve accident prevention measures, the company shared its detailed five-year (2016-2020) plan to enhance safety measures and raise long-term awareness. Key performance indicators for division heads now include health and safety measures.</li><li>› PSP Investments continues to encourage the company to improve its health and safety management.</li></ul>	

## Large international oil and gas company

### ENGAGEMENT OBJECTIVE

Enhance disclosure regarding stranded asset risk.

### BACKGROUND

As with other major oil and gas producers, the company is potentially exposed to a reduction in long-term demand because of climate change mitigation policies.

The company could over-invest in exploration and production. This could undermine returns on investment and lead to asset write-downs. Some assets could become stranded and cease to operate.

### ACHIEVEMENTS

- › Investors sent a letter requesting information about the potential risk of stranded assets. The company acknowledged shareholder concerns in theory, but did not make its position public.
- › Through engagement, investors continued to pressure the company and, in 2014, it publicly released a letter stating that climate warming is likely to exceed 2 °C by the end of the 21<sup>st</sup> century.
- › Since 2015, we have held several meetings with the company to highlight the importance of enhanced climate-related risk disclosure. It has publicly acknowledged that reduced demand in low-carbon scenarios could impact some business activities, but said demand for energy efficient products could increase for gas, biofuels and chemicals.

## Oil and gas company

### ENGAGEMENT OBJECTIVES

Increase Board independence.

Ensure better Board representation for minority shareholders.

Reduce conflict of interest and address identified corruption-related risks.

### BACKGROUND

This state-controlled company has minority shareholders, including international institutional investors. An ongoing investigation, initiated in 2009, uncovered a corruption scandal in which politically-appointed executives were accused of extracting bribes from suppliers and contractors. We were concerned by the lack of mechanisms to manage and mitigate the government's conflict of interest.

### ACHIEVEMENTS

- › In 2012, we began to engage with the company on Board composition. We proposed changes to allow minority shareholders to nominate and elect two independent directors. The proposal was initially rejected by government-backed shareholders, including state-controlled pension funds.
- › Our engagement on Board representation, in collaboration with other institutional investors, has been successful. At the company's 2015 annual general meeting—as the ongoing investigation into corruption intensified—the government nominated two independent directors, instead of government officials, to serve on the Board. The company also appointed a Chief Compliance Officer to strengthen the corporate governance framework. In addition, it established a dialogue with minority shareholders, helping to significantly improve corporate governance practices. A robust compliance and cultural change management program is underway.
- › We are monitoring the company's progress, providing feedback and sharing best practices. A formal nomination policy with stringent integrity requirements for Board and senior management appointments has also been developed.

## North American healthcare company

### ENGAGEMENT OBJECTIVES

Board structure: Board member renewal; separation of Board Chair and CEO roles.

Executive compensation: Strengthen clawback policy and improve clarity of performance conditions for incentive awards.

Adoption of proxy access.

### BACKGROUND

In 2012, we initiated engagement with the company to raise concerns about governance-related issues.

On executive pay, we were concerned about a weak clawback policy and the lack of clarity regarding performance conditions attached to incentive awards.

On Board structure, we were concerned about the combined roles of Board Chair and CEO, and the number of long-tenured Board members.

We offered counsel regarding the adoption of proxy access and general governance disclosures.

### ACHIEVEMENTS

The company is now recognized in North America—and globally—for best practices for its governance structure and investor engagement activities.

The company has improved its practices regarding Board structure and composition, executive pay, proxy access and shareholder engagement:

- › Board structure: Appointment of the lead independent director position with a robust and clear set of powers coupled with changes strengthening the Board's leadership structure and committee membership.
- › Board refreshment and diversity: Three new independent directors were recently appointed. In 2016, the company was recognized by the 2020 Women on Boards campaign; more than a fifth of Board members are women.
- › Significant improvements to executive compensation: The company introduced longer-term incentive plans for executives with a clear link to company performance. The clawback policy is recognized as an industry best practice.
- › In 2015, the Board proposed the adoption of a proxy access bylaw: It would allow shareholders holding an aggregate of at least 3% of outstanding shares, for a minimum period of three years, to use proxy materials to nominate up to 20% of Board candidates.
- › The Board and management expanded investor engagement efforts.