

**IN  
VEST  
ING**

**RESPONSIBLY**

PUBLIC SECTOR  
PENSION INVESTMENT BOARD  
**2017 RESPONSIBLE INVESTMENT REPORT**



## WHO WE ARE

The Public Sector Pension Investment Board (PSP Investments) is one of Canada's largest pension investment managers, with \$135.6 billion of net assets under management as of March 31, 2017.

We are a Canadian Crown corporation that invests funds for the pension plans of the federal public service, the Canadian Forces, the Royal Canadian Mounted Police and the Reserve Force. Our headquarters are located in Ottawa and our highly-skilled and diverse team of more than 700 professionals works from offices in Montréal, New York and London.

## WHAT WE DO

PSP Investments' mandate is to manage the pension funds transferred to it by the Government of Canada in the best interests of contributors and beneficiaries, and to maximize investment returns without undue risk of loss.

To that end, we manage a diversified global portfolio of stocks, bonds and other fixed-income securities, and pursue private investments in private equity, real estate, infrastructure, natural resources and private debt.

## OUR VISION

Our vision is to be a leading global institutional investor that reliably delivers on its risk-return objective by focusing on a total fund perspective and always acting in the best interests of our Canadian sponsor and pension plan contributors and beneficiaries. As we pursue a larger global footprint, we will leverage our talent to deliver efficient execution at scale and become an agile and sought-after enabler of complex global investments.

## TABLE OF CONTENTS

---

1	<b>Responsible Investment</b>	7	Private Markets	12	Public Markets	21	<b>Working with Others to Effect Change</b>
2	<b>President's Report</b>	8	<i>Real Estate</i>	16	Engaging with Public Companies	25	<b>Taking a Stance on Public Policy</b>
4	<b>Laying the Groundwork</b>	9	<i>Natural Resources</i>				
6	<b>Supporting All Investment Groups</b>	9	<i>Infrastructure</i>				
		10	<i>Private Equity</i>				
		11	<i>Private Debt</i>				

# RESPONSIBLE INVESTMENT

At PSP Investments, we believe that responsible corporate behaviour with respect to environmental, social and governance (ESG) factors generally has a positive influence on long-term financial performance.

We take a pragmatic view when applying our approach to responsible investing. This approach is tailored to local social and legal environments, and to the commercial imperatives of the companies in which we invest. We expect these companies to comply with the legal and regulatory regimes applicable to them.



# TURNING ESG RISKS INTO OPPORTUNITIES



WE ARE EXTREMELY PROUD  
TO PRESENT YOU WITH OUR  
INAUGURAL RESPONSIBLE  
INVESTMENT REPORT.

At PSP Investments, we know that environmental, social and governance (ESG) factors have a direct impact on both risk and long-term profitability.

If there is one takeaway from this report, it is that responsible investment is at the very core of our investment strategy.

## A TOTAL FUND PERSPECTIVE

Our responsible investment approach is aligned with our total fund perspective. It is rooted in the belief that good corporate conduct and strong governance enhance long-term financial performance. Our approach is inspired by our shared purpose to act in the best interests of pension plan contributors and beneficiaries – the men and women who have served Canada throughout their careers.

As in our business strategy, we count on our partnerships with like-minded organizations for responsible investment success. Our definition of success goes beyond mere financial considerations. It means acting as a corporate steward to create long-term, sustainable value for *all* of our stakeholders.

We approach ESG from a double-edged perspective: risks and opportunities. Rather than simply noting investment risks in our assessments, we view them as value-creation opportunities, and we work closely with our partners to unlock the value they present.

I encourage you to read about our many important successes throughout fiscal year 2017, from supporting a major oil and gas company to enhance transparency, to helping to improve the health and safety practices of an Asian semiconductor manufacturer. You will also discover how we work with many world-class ESG-related associations, such as the UN-supported Principles for Responsible Investment and the Canadian Coalition for Good Governance.

## A STRATEGICALLY LOCATED TEAM

To fulfill our responsible investment mandate, in the last fiscal year, we built a dedicated seven-member team. Led by Stéphanie Lachance, Vice President, Responsible Investment, the team is housed within the Chief Investment Officer Group for a clear view across the organization. It analyzes investments and works with all of our asset classes to manage ESG factors. This supports our belief that, as a long-term investor, establishing strong responsible investment oversight is not only necessary for value creation – it is the right thing to do.

I would like to thank the Responsible Investment group for their invaluable contribution to our organization, and I would like to thank all employees for their continued commitment to helping PSP Investments incorporate ESG into all of our activities.



André Bourbonnais  
President and Chief Executive Officer

# LAYING THE GROUNDWORK

## BUILDING A MULTIDISCIPLINARY TEAM

**When PSP Investments created a group dedicated to responsible investment in June 2016, we expanded our in-house capabilities in respect to ESG matters.**

The Responsible Investment group is composed of seven members and is led by Stéphanie Lachance, Vice President, Responsible Investment. The members of this multidisciplinary team have diverse backgrounds and support our investment groups in both public and private markets.

The Responsible Investment group is dedicated to integrating ESG factors in the decision making processes across all asset classes so they are considered more broadly and consistently within our organization, as articulated in PSP Investments' [Responsible Investment Policy](#). The Responsible Investment group reports bi-annually on its activities to the Governance Committee of PSP Investments' Board of Directors.

## DEVELOPING THE ROADMAP

**In fiscal year 2017, with the support of the Board and senior management, we developed a detailed roadmap for our key initiatives and projects.**

*“When we created our Responsible Investment group, we knew the logical home for it was within the CIO Group. This was a very strategic decision for us. It allows our RI group to have a full-spectrum view across all asset classes and investment groups, and RI to be an integral part of total portfolio considerations. Bottom line? It builds RI into the foundation of everything we do.”*

— Daniel Garant – Executive Vice President and Chief Investment Officer

**PSP Investments' RI activities are articulated around four key pillars :**

- › Policy development and strategy
- › Advisory role to the Board, President and CEO, and investment groups
- › Responsible investment oversight
- › ESG training

KEY ACHIEVEMENTS IN FISCAL YEAR 2017

**PILLAR** POLICY DEVELOPMENT AND STRATEGY

OBJECTIVES	FISCAL YEAR 2017 ACHIEVEMENTS
<p>Develop responsible investment policy and strategic initiatives.</p> <p>Monitor ESG themes and measure risks for each asset and sub-asset class, and on a total portfolio basis.</p>	<ul style="list-style-type: none"> <li>- Adoption of the Responsible Investment group roadmap detailing our strategy, activities, key initiatives and projects.</li> <li>- Portfolio monitoring in respect to ESG themes, such as board diversity and climate change.</li> <li>- Promotion of greater gender diversity on the boards of TSX listed issuers.</li> </ul>

**PILLAR** ADVISORY ROLE TO THE BOARD, PRESIDENT AND CEO, AND INVESTMENT GROUPS

OBJECTIVE	FISCAL YEAR 2017 ACHIEVEMENTS
<p>Provide advice and guidance to the Board, the President and CEO, and investment groups on ESG trends and practices to ensure they form part of the investment decision making process.</p>	<ul style="list-style-type: none"> <li>- Systematic ESG assessment by the Responsible Investment group for all significant private market transactions.</li> <li>- Implementation of general partner and external manager interview processes to foster adoption of sound ESG practices.</li> </ul>

**PILLAR** RESPONSIBLE INVESTMENT OVERSIGHT

OBJECTIVE	FISCAL YEAR 2017 ACHIEVEMENTS
<p>Pursue active ownership through proxy voting and engagement activities with public issuers.</p>	<ul style="list-style-type: none"> <li>- Refinement of our proxy voting-related activities.</li> <li>- Development of in-house capabilities to engage portfolio companies on their ESG practices and performance.</li> </ul>

**PILLAR** ESG TRAINING

OBJECTIVE	FISCAL YEAR 2017 ACHIEVEMENTS
<p>Increase internal capabilities so ESG factors are adequately considered during the investment decision making process.</p>	<ul style="list-style-type: none"> <li>- Delivery of internal training sessions in respect of ESG activities and integration across asset classes.</li> <li>- ESG subject matter presentations at conferences and to external parties.</li> </ul>

In fiscal year 2018, we will continue to refine our approach to responsible investment in support of PSP Investments' five-year corporate strategy, Vision 2021.

# SUPPORTING ALL INVESTMENT GROUPS



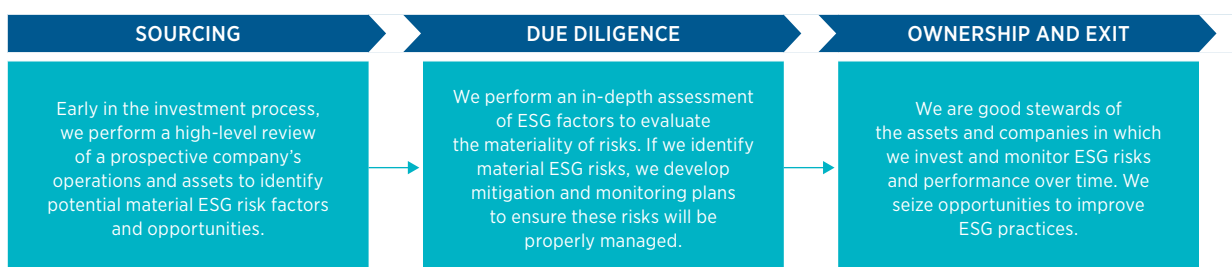


# PRIVATE MARKETS

We work to identify ESG risks in our real estate, natural resources, infrastructure, private equity and private debt investments. Risks include those linked to climate change, other environmental issues, health and safety, human rights and business ethics.

ESG risk analysis is fundamental to our due diligence process and is addressed in each investment recommendation submitted to the Board of Directors' Investment Committee, the President and CEO, and other approving officers. Our investment teams monitor ESG factors throughout the life of investments and implement mitigation measures when risks are identified. In fiscal year 2017, we decided not to pursue certain investment opportunities due to heightened ESG risks which could not be properly mitigated.

## INTEGRATING ESG CONSIDERATIONS AT EACH STEP OF THE INVESTMENT CYCLE



The ESG integration process outlined above varies according to asset class and type of investment. For example, we make a significant portion of our investments through funds. Fund managers are responsible for both the selection and monitoring of portfolio companies. We engage with fund managers to ensure their respective approaches to ESG integration are consistent with our Responsible Investment Policy.

**In fiscal year 2017, for the selection of all new fund managers, we supplemented our ESG due diligence questionnaire with systematic interviews of fund managers to further assess their ESG practices.**



We are directly invested in approximately 1,100 properties around the world. The Real Estate group favours direct ownership and co-ownership through joint ventures with operating partners that are aligned to create value and generate returns.

In fiscal year 2017, the Responsible Investment group supported PSP Investments' real estate partners on a variety of ESG-related initiatives. These included the preparation of guidance and tools for developing a responsible investment policy for our real estate partners and the development of enhanced corporate governance structures for our emerging markets activities. It is a challenge for institutional investors, like PSP Investments, to measure the ESG performance of a large property portfolio. But we are actively evaluating various alternatives for doing so — in accordance with best practices.

*“ESG considerations are fundamental to all of our real estate and natural resources investment and asset management decisions. We take into account regulation and market forces, including future societal trends and preferences, in determining markets and assets in which to invest, and to define and implement recognized best practices in investment operations and decision making.”*

— Neil Cunningham, Senior Vice President, Global Head of Real Estate and Natural Resources

## Responsible investment in action

### Survey of real estate partners

- › In fiscal year 2017, the Responsible Investment group surveyed a sample of real estate partners, representing more than 80% of our directly owned properties, about their ESG practices.
- › More than 90% of properties that underwent development or major renovations during the fiscal year included ESG initiatives. Initiatives included projects to improve energy and water efficiency, waste management and health and safety factors, as well as the use of sustainable construction materials.
- › Some properties were assessed using green building certification schemes or ratings, such as Leadership in Energy and Environmental Design (LEED), Building Research Establishment Environmental Assessment Method (BREEAM), National Australian Built Environment Rating System (NABERS) and Energy Star®.
- › Several properties implemented ESG targets, such as energy reduction, water efficiency, waste diversion and engagement with tenants on environmental and social initiatives.

## NATURAL RESOURCES

The Natural Resources group invests primarily in real assets and other opportunities in timber and agriculture.

Given the high exposure of natural resources investments to weather conditions, we perform climate change risk assessments as part of our investment due diligence. In fiscal year 2017, we assessed the ongoing impact of climate change on crop yields and agricultural property operations on several continents. Climate change parameters include the frequency and severity of extreme weather events, occurrence of colder temperatures, precipitation levels and water availability.

### *Responsible investment in action*

#### **TimberWest: In 2011, PSP Investments acquired a 50% interest in TimberWest.**

TimberWest is western Canada's largest private timberland company and has been in operation for over 100 years.

In 2016, TimberWest undertook a number of outreach initiatives with local communities in British Columbia. It worked with First Nations and environmental groups to help pass the Great Bear Rainforest Land Use Order. The company also contributed to funding construction of the Vancouver Island link in Canada's Great Trail project.

In addition, we supported an assessment of TimberWest's health and safety performance. Following that, the company implemented a health and safety improvement action plan for both itself and its subcontractors.

## INFRASTRUCTURE

The Infrastructure group invests globally on a long-term basis, primarily in the transportation, power generation, telecommunications and public utilities sectors. The group is focused on direct investments, including platforms and co-investments.

Given the long-term investment horizon for infrastructure assets, their environmental and social impacts must be properly assessed and managed.

### *Responsible investment in action*

#### **Alpha Trains: In 2008, PSP Investments acquired a minority interest in Alpha Trains.**

Alpha Trains is continental Europe's largest and most diversified specialist train leasing company. It provides almost €2.5 billion in new-build rolling stock to both public and private operators in a dozen European countries.

In late 2016, Alpha Trains issued a €250 million Green Private Placement, a first for a rolling stock leasing company. The issuance was certified by the Climate Bond Initiative as compliant with the International Capital Markets Association's Green Bond Principles for Low Carbon Land Transport. At the Climate Bonds 2017 Conference, Alpha Trains received a Green Bond Pioneer Award for its green bond issuance. This was a significant achievement: it highlights Alpha Trains' efforts to act as a responsible investor in low-carbon assets, and contribute to achieving European Union greenhouse gas reduction targets.

## PRIVATE EQUITY



Private Equity focuses on constructing a diversified portfolio across sectors and geographies by strategically building relationships with external funds and investing partners to source long-term direct investment and co-investment opportunities.

*“The Responsible Investment group provides valuable input to our investment teams in assessing long-term risks and opportunities, and offers critical support in our investment due diligence review process.”*

— Guthrie Stewart, Senior Vice President and Global Head of Private Investments.

### *Responsible investment in action*

**TeamHealth: In early 2017, PSP Investments acquired a minority interest in TeamHealth at the time of its privatization.**

TeamHealth is one of the largest physician staffing organizations in the United States. It supplies outsourced healthcare professional staffing and administrative services to hospitals and other healthcare providers. TeamHealth is exposed to ESG risks and opportunities that could have a material influence on its operations and financial position. Risks relate to the quality of care and patient satisfaction, ethics, and employee development and retention.

As part of our investment due diligence process, we thoroughly assessed TeamHealth’s ESG practices and noted that the company had implemented several programs that led to industry recognition, including:

- › In February 2017, for a third consecutive year, TeamHealth was named in Fortune magazine’s *List of the World’s Most Admired Companies* based on social responsibility, global competitiveness, quality of services and people management criteria.
- › In March 2017, for a third consecutive year, TeamHealth was listed in Becker’s Hospital Review of 150 Great Places to Work 2016, with mention of its clinician continuing medical education and training programs, and its new Women in Leadership program.

## PRIVATE DEBT



Private Debt focuses on direct non-investment grade primary and secondary credit investments in North America and Europe. It has the ability to commit to large positions and different portions of the debt capital structure in both loan and bond form.

As a lender, PSP Investments' ability to influence company ESG practices becomes more limited once a debt investment is made. Through our private debt investment due diligence review process, we aim to ensure that companies have implemented adequate procedures to manage and mitigate material ESG risks.

*"Our Private Debt group must respond quickly to investment opportunities. We need to be agile. The Responsible Investment group provides the fast turnaround we need in terms of tools and advice to assess the ESG risks associated with potential capital deployment."*

— David J. Scudellari, Senior Vice President, Head of Principal Debt and Credit Investments

### *Responsible investment in action*

#### **Industrial cleaning company**

In 2016, PSP Investments reviewed a private debt investment opportunity for a US-based industrial cleaning company. Environmental, health and safety (EH&S) factors presented potential material risks to the company's operations. With assistance from an expert advisor, we conducted a due diligence process that included an in-depth assessment of the company's EH&S practices.

The Responsible Investment group conducted management interviews, reviewed documentation and an expert advisor made onsite visits to confirm the company had robust systems to address key EH&S risks relating to waste water, air emissions and chemical storage. We noted that a dedicated team oversees these systems and has responsibility for policies, procedures, employee training, auditing, and compliance and performance monitoring. Our review concluded that the company has the capacity to manage key risks and to improve EH&S performance over time.

# 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.

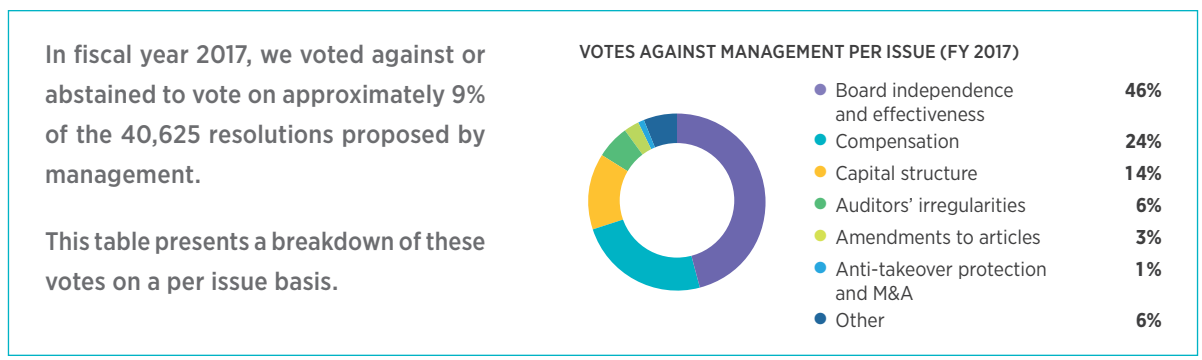
With regards to our active management of proxy voting:

- › 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



## 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

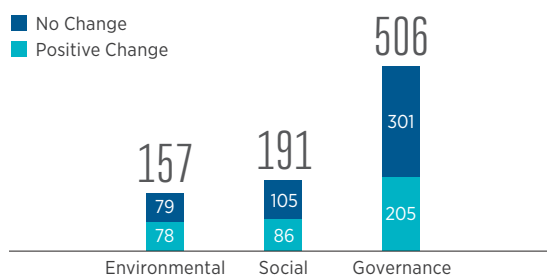


*“Our Responsible Investment group takes a proactive role when engaging with companies and peer organizations on environmental, social and governance issues. The group favours dialogue and collaboration, and its efforts produce tangible results. For example, in fiscal year 2017, its interventions with 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	
<p><b>ENGAGEMENT OBJECTIVE</b></p> <p>Ensure better alignment of Board composition with the company's strategy.</p>	<p><b>BACKGROUND</b></p> <p>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.</p>
<p><b>ACHIEVEMENTS</b></p> <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	
<p><b>ENGAGEMENT OBJECTIVE</b></p> <p>Improve health and safety practices.</p>	<p><b>BACKGROUND</b></p> <p>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.</p>
<p><b>ACHIEVEMENTS</b></p> <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.

# WORKING WITH OTHERS TO EFFECT CHANGE

## PSP INVESTMENTS' MEMBERSHIPS AND COLLABORATIONS



We work with a number of organizations to support initiatives that enhance the quality of ESG practices and disclosure.

For PSP Investments, responsible investing means being committed to principles and collaborating with peers to support robust and vibrant financial markets. We promote sound governance practices, meaningful non-financial disclosure, effective boards and companies, and good public policy. As part of our commitment, we are proud to partner with our peers, investment partners, industry associations, regulators and standard setters.

**In March 2017, PSP Investments hosted Canada's first ESG peer forum at which leading Canadian pension funds discussed issues ranging from proxy voting to ESG best practices in private markets.**



## UNITED NATIONS SUPPORTED PRINCIPLES FOR RESPONSIBLE INVESTMENT (PRI)

The PRI is the world's leading proponent of responsible investment. It examines the investment implications of environmental, social and governance factors, and supports its international network of investor signatories in incorporating these factors into their investment and ownership decisions. Signatories are required to report annually on their responsible investment activities by filing a PRI Transparency Report, detailing their responsible investment and ESG integration activities.

PSP Investments' PRI Transparency Report is available at the PRI website.

## PRI QUÉBEC NETWORK

PSP Investments is a member of the PRI Québec Network, which encourages the adoption of the Principles for Responsible Investment by Québec-based financial market participants.

## PRI ADVISORY COMMITTEE ON CREDIT RATINGS (ACCR)

PSP Investments is a member of the ACCR, whose objective is to advise PRI on its program to promote more systematic and transparent incorporation of ESG factors in credit ratings and assessments. The ACCR aims to raise awareness and understanding of the links between ESG factors and issuer creditworthiness among credit analysis and ratings professionals, and to improve understanding of different approaches to ESG integration in credit analysis.



## OUR ACTIONS IN SUPPORT OF PRI PRINCIPLES

PRINCIPLES	ACTIONS TAKEN AT PSP INVESTMENTS
<b>PRINCIPLE 1</b> We will incorporate ESG issues into investment analysis and decision making processes.	We analyze the risks inherent in any investment in order to identify, monitor and mitigate ESG issues that are/could become material to long-term financial performance. ESG risks are part of the due diligence process of potential investments across asset classes.
<b>PRINCIPLE 2</b> We will be active owners and incorporate ESG issues into our ownership policies and practices.	In fiscal year 2017, we voted on 41,912 resolutions presented in 3,871 meetings. In fiscal year 2017, we engaged directly with 477 public companies on issues ranging from board independence, health and safety to climate change. We monitor ESG factors throughout the life of all investments and implement mitigating measures when risks are identified.
<b>PRINCIPLE 3</b> We will seek appropriate disclosure on ESG issues by the entities in which we invest.	We are a signatory to the CDP and CDP Water Program. Improvement of ESG disclosure is one of our standard engagement objectives with public companies. We support various shareholders' proposals requesting additional ESG disclosure.
<b>PRINCIPLE 4</b> We will promote the PRI acceptance and implementation in the investment industry.	We participate in several collaborative organizations and initiatives. We are an active member of various PRI committees, including the Québec PRI Network and the PRI Advisory Committee on Credit Ratings. We are a founding member of Finance Montréal's Responsible Investment Work Group that promotes responsible investment within Montréal and Québec's financial community. As part of our review and due diligence process, we encourage external managers and partners to adopt ESG best practices and to become a PRI signatory.
<b>PRINCIPLE 5</b> We will work together to enhance our effectiveness in implementing the PRI.	We collaborate with Canadian peers and like-minded global investors to more effectively deploy resources and encourage change. In fiscal year 2017, we spearheaded and hosted the first ESG peer forum for leading Canadian pension funds. The forum aims to advance and promote ESG best practices.
<b>PRINCIPLE 6</b> We will each report on our activities and progress toward implementing the PRI.	We are committed to reporting on our responsible investment activities, as evidenced by this inaugural annual standalone Responsible Investment Report and the annual filing of our PRI Transparency Report.

## PENSION INVESTMENT ASSOCIATION OF CANADA (PIAC)

PSP Investments is a member of PIAC, whose mission is to promote sound investment practices and good governance for the benefit of pension plan sponsors and beneficiaries. PIAC is a forum in which Canadian pension funds share information and knowledge.



We are an active participant in PIAC's Investor Stewardship Committee. It aims to develop, monitor and promote robust standards and best practices for pension investment stewardship in Canada. The committee focuses on proxy voting, corporate engagement, corporate governance, the integration of ESG factors into the investment process, and advocacy with public policy makers and standard setters.

## FINANCE MONTRÉAL

PSP Investments is a member of Finance Montréal's Responsible Investment Work Group. Finance Montréal is a financial cluster whose mission is to develop and promote Québec's financial services industry.



**André Bourbonnais, PSP Investments' President and CEO, accepted to lead Finance Montréal's Responsible Investment Work Group. The group is tasked with identifying strategic projects to develop responsible investment practices in Montréal's financial community.**

## 30% CLUB

In June 2016, PSP Investments became a member of the 30% Club. We joined our voice with others who believe that gender balance on boards and at senior management levels encourages better leadership and governance, and that diversity contributes to better, all-round board and corporate performance. The 30% Club's mission is to develop a diverse pool of talent for all businesses through the efforts of its Chair and CEO members who are committed to better gender balance at all levels of their organisations.



The 30% Club does not believe in mandatory quotas. Instead, it supports a voluntary approach to meaningful, sustainable change. However, it has set a 2019 target of 30% of board seats to be held by women.

**In 2016, we wrote to approximately 50 TSX-listed issuers that had no female representation on their boards. Using our voting rights, we have exerted pressure on companies with no female board representation by voting against their nominating committees and governance committee chairs. With other Canadian pension funds, we have identified the promotion of more diverse boards as an area for greater collaboration.**

## CANADIAN COALITION FOR GOOD GOVERNANCE (CCGG)

The CCGG represents institutional investors with approximately \$3 trillion in assets under management. On behalf of its members, the CCGG engages with the boards of directors of as many as 50 Canadian public issuers to discuss topics such as corporate governance.



**Stéphanie Lachance, PSP Investments' Vice President, Responsible Investment, is a CCGG Board member and chairs its Member Engagement Committee.**

PSP Investments supports CCGG's efforts in respect to the adoption of proxy access in Canada. We believe proxy access is a meaningful way for shareholders to have a say in the director nomination process. It is an essential component of shareholder democracy, as existing Canadian corporate statutes and applicable securities laws do not provide for effective proxy access mechanisms.

## INTERNATIONAL CORPORATE GOVERNANCE NETWORK (ICGN)

ICGN promotes effective standards of corporate governance and investor stewardship to advance efficient markets and sustainable economies worldwide. As an ICGN member, PSP Investments supports its Global Governance Principles and Global Stewardship Principles which aim to:



- › Influence policy by providing a reliable source of investor opinion on governance and stewardship.
- › Connect peers to enhance dialogue between companies and investors on long-term value creation.
- › Inform dialogue through knowledge and education to enhance the professionalism of governance and stewardship practices.

## CDP

PSP Investments is a signatory of CDP (formerly known as the Carbon Disclosure Project). CDP acts on behalf of 827 institutional investors with more than US\$100 trillion in assets under management. The CDP sends an annual questionnaire to the world's largest publicly listed companies and encourages them to disclose how they manage climate change-related risks and opportunities. PSP Investments is also a signatory to the CDP Water Program, which enables institutional investors to access high-quality information about the investment risks and opportunities associated with water scarcity and other water-related issues.



# TAKING A STANCE ON PUBLIC POLICY

As an institutional investor, we believe that efficient and vibrant financial markets are essential to achieving our investment mandate. We are involved in many initiatives that aim to protect the integrity of the market and shareholders' rights.

## CANADIAN SECURITIES ADMINISTRATORS

PSP Investments has been working with its Canadian peers to improve and adopt industry protocols to strengthen Canada's proxy voting infrastructure. These efforts have culminated in the publication by the Canadian Securities Administrators (CSA) of CSA Staff Notice 54-305: Meeting Vote Reconciliation Protocols. The Protocols outline CSA staff expectations of, and guidance for, improving the processes involved in proxy vote tabulations.

PSP Investments maintains an ongoing dialogue with the CSA and other regulatory authorities to introduce mandatory "say-on-pay" in Canada. We believe that Canada should be more closely aligned with the executive compensation practices of other jurisdictions. Canada is one of the few developed countries with a voluntary and non-binding "say-on-pay" system. This deprives shareholders of many Canadian companies of the opportunity to express their opinions about executive pay and performance, limiting them to potentially more drastic measures (i.e. selling their shares, voting against the re-election of directors or pursuing a more activist agenda).

## LISTINGS ADVISORY COMMITTEE, TORONTO STOCK EXCHANGE (TSX)

PSP Investments is a long-standing member of the TSX's Listings Advisory Committee. The Committee is composed of individuals representing participating organizations, institutional investors and issuers who are drawn from diverse backgrounds, including the legal, business, accounting and regulatory professions.

The committee provides advice on general regulatory and business issues relating to TSX listings, including:

- › Public interest rule amendments prior to publication.
- › Initiatives and issues, which may include general requirements relating to both original and continued listings, and listed issuers' standards and policies.

## CLIMATE CHANGE DISCLOSURE

Companies are not mandated to disclose quantitative and qualitative climate-related information. However, investors need this information to properly manage the risks related to climate change and the potential impacts on the long-term financial performance of their investments. Unfortunately, disclosures are not yet available for a significant portion of our investments, nor are there mature tools to analyze climate-related investment risks.

### **Task Force on Climate-related Financial Disclosures (TCFD)**

PSP Investments commented on the draft recommendations issued by the TCFD. The TCFD was established in 2016 by the Financial Stability Board to develop recommendations in order to promote consistent, comparable, reliable, clear and efficient climate-related financial disclosures. The TCFD recommendations will help investors to access information on investment risks related to climate change.

# DEDICATED TO MAKING A DIFFERENCE

In fiscal year 2018, we will continue to reinforce our ESG practices and deliver projects and initiatives to enhance responsible investment across all asset classes. We will report on our progress in our second standalone Responsible Investment report.

## WE ARE LISTENING

If you have any questions or comments, please contact us at:  
[responsibleinvestment@investpsp.ca](mailto:responsibleinvestment@investpsp.ca)



[responsibleinvestment@investpsp.ca](mailto:responsibleinvestment@investpsp.ca)

**BUSINESS OFFICES**

**MONTREAL**

(Main office)

1250 René-Lévesque Blvd. West, Suite 1400

Montréal, Québec H3B 5E9

Canada

T. +1 514.937.2772

**NEW YORK**

450 Lexington Avenue, Suite 3750

New York, NY 10017

USA

T. +1 212.317.8879

**LONDON**

10 Bressenden Place

8<sup>th</sup> floor

London, United Kingdom

SW1E 5DH

T. +44 20 37 39 51 00

**HEAD OFFICE**

**OTTAWA**

1 Rideau Street

7<sup>th</sup> floor

Ottawa, Ontario K1N 8S7

Canada

T. +1 613.782.3095

[info@investpsp.ca](mailto:info@investpsp.ca)