



# 2022 PROXY VOTING GUIDELINES

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# GENERAL PRINCIPLES

Common stock usually carries voting rights. Voting rights are valuable assets and trustees have an obligation to ensure that votes attached to shares owned by their fund are voted in a way that supports the interests of purpose of the organization over the long term.

## Duties of loyalty and care

The trustees of the fund and anyone appointed to vote proxies on the trustees' behalf have a duty of loyalty to exercise their proxy voting authority solely in the interests of the trust's beneficiaries. They have a duty of care to exercise their proxy voting authority with the prudence, skill, and diligence that a prudent person would exercise in managing the property of others. Failing to vote the plan's shares, voting without consideration of the effects of the vote, or voting arbitrarily with or against management violates these duties. Those who are responsible for voting also have a duty to take reasonable steps to ensure that they receive and act on the proxies for all shares in a timely manner.

## Application of these guidelines

In deciding how to apply the guidelines, the circumstances of each vote as well as the general principles contained in these guidelines, will be considered. The overarching principle in interpreting and applying these guidelines is to follow the course of action that will best serve the long-term interests of beneficiaries, in a manner that is consistent with the duties of loyalty and care, and that supports implementation of current best practices in corporate governance and social responsibility.

Voting decisions may deviate from these guidelines if doing so would best serve beneficiaries' interests in the long term. If questions arise about the application or interpretation of these guidelines for any issue, they should be resolved in consultation between the voting agent and the staff and trustees of the fund.

## Recognize systemic risks

In addition to assessing how each vote will affect issuers individually, votes should also be assessed for their impact on economy-wide systemic issues that may affect our portfolio and its future investment returns. Investment returns come primarily from the performance of capital markets and the economy. Market-wide standards of corporate behaviour are an important contributor to investment outcomes. Voting should be assessed for its impact on the economy, and on the society and environment upon which it depends.

# THE RESPONSIBLE COMPANY

Companies do not operate in a vacuum. They affect and are affected by the people, social structures, and environment around them. International and domestic law and convention establish varying degrees of corporate responsibility for the effects of a corporation's conduct on its stakeholders such as employees, shareholders, lenders, customers and suppliers, the communities in which they operate, and on the natural environment. But responsible business conduct is not solely a matter of legal liability. It is inseparable from good business practice and good corporate governance, because it affects a company's ability to operate profitably and sustainably in the long term.

[The fund] supports the development of strong corporate governance and responsible business conduct as a means of promoting long-term value and a sustainable, inclusive, and productive economy.

## Responsible business conduct and good governance

The standards for good corporate governance around the world tend to be more alike than are the legal requirements and norms for corporations in different countries. [The fund] will not ignore the laws and norms of the countries in which companies operate, but it has chosen to apply these guidelines consistently in all countries. If a guideline addresses an issue that appears only in certain jurisdictions or if different standards apply based on jurisdiction, this is stated in the relevant guideline.

International law and standards provide useful guidance for evaluating responsible business conduct. [The fund] will be guided in its proxy voting by the principles that are expressed in the following international standards.

- The Universal Declaration of Human Rights
- The ILO Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy
- The OECD Guidelines for Multinational Enterprises
- The UN Declaration on the Rights of Indigenous Peoples
- The UN Global Compact
- The UN Guiding Principles on Business and Human Rights

The primary responsibility for determining how a company implements responsible business practices rests with management. However, when a company's actions violate international standards or expose the company to increased risk, fiduciaries have a responsibility to protect the value of their investments.

- In general, [the fund] will vote for shareholder proposals that call on companies to adhere to principles established in these international standards.

# OVERSIGHT BODIES OF THE COMPANY

## GENERAL GUIDELINES

Good corporate governance is based on the relationships between a company's board of directors or supervisory board, its management, and its other stakeholders, including its shareholders, employees, and the citizens of the countries where it operates. Shareholders, as the providers of the company's equity capital, elect the board of directors and have other rights that give them a voice in aspects of the board's operations. The board of directors is elected by the shareholders and is accountable to them. The board controls the company's assets and actions, and it is responsible for overseeing the work of management. Management is responsible for running the company and is accountable directly to the board. The relationships among these bodies are key to a company's long-term success.

## BOARDS OF DIRECTORS

There are two general types of corporate board structures. Some companies have a unitary board structure, in which a single board of directors is responsible for overseeing the management of the company on behalf of its shareholders.

Other companies have two boards. The role and makeup of the boards at dual-board companies varies with the jurisdiction. In some jurisdictions, companies have a board of directors like the board of a unitary company, and a second board of statutory auditors who are formally responsible for ensuring that the company's acts are legal and/or that the annual audit is properly conducted. Companies in other jurisdictions are governed by a board of supervisors that often includes employees' representatives, and a management board. The board of supervisors chooses the management board, which includes the executive officers and is responsible for running the company.

The guidelines below are applicable to all these types of boards.

### Board expertise

As demands grow for companies to operate sustainably, boards may find that they need directors who have social and environmental expertise that is not traditionally valued.

- [The fund] will vote for proposals to add qualified directors to corporate boards who have expertise in areas that the board needs and lacks, such as climate change, biodiversity, human rights and equity.

### Voting for directors and the independence of the board

- [The fund] will vote case-by-case for directors. In addition to reasons listed in the following sections, votes may be withheld or cast against management's nominees if:
  - The board of directors has not acted on issues that have the support of most shareholders or given an appropriate response to shareholders' concerns. This includes management proposals that a majority of shareholders vote against.
  - The board of directors has taken steps to limit shareholders' rights without shareholders' approval, such as by adopting an exclusive forum requirement or advance notice requirements.
  - The board of directors consistently acts in the interests of a group of shareholders rather than in the interests of all shareholders.
  - An individual director is not qualified to be a corporate director, or the company has not disclosed adequate information about the director's qualifications.



- An individual director has a conflict of interest; a conviction for financial, corporate, or securities crime, including insider trading; or a history of serious misconduct, regulatory sanctions, or ethical violations relating to corporate responsibilities.
- There is evidence that directors have purposely misstated or concealed the financial condition of the company.
- The board has regularly demonstrated a lack of duty of care, such as approving corporate restructurings that are not in the company's best interests or refusing to provide information to which shareholders are entitled.
- The board has not carried out its responsibilities in a way that protects the value of the company but does not qualify as failing in its duty of care. Examples are poor employee relations that result in costly strikes, or substantial fines or legal costs that result from violating laws or regulations.
- An individual director has served on the board of another company that has demonstrated a particularly egregious failure in its duty of care, and the board has not provided a convincing justification for including this director on the board.
- If less than two-thirds of directors are independent as defined by these guidelines, vote against non-independent directors.
- [The fund] will vote for proposals to require two-thirds of directors to be independent.
- [The fund] will vote for proposals to require annual disclosure of which directors are independent and the basis on which the assessment was made.

[The fund] might vote against a nominee for director for many other reasons. These are addressed in the following sections.

### Majority vote for elections of directors

Shareholders of most Canadian companies cannot vote against directors. Proxy ballots only allow shareholders to vote “for” or “withhold” for director nominees. The result is that unless a nominee receives no votes, all directors who are nominated are elected regardless of how many “withhold” votes they receive.

The Toronto Stock Exchange requires all listed companies to hold majority elections for directors.<sup>1</sup> Majority elections require a director to win a majority of the votes cast in order to be elected to the board. They effectively turn “withhold”

votes into votes against a nominee and make it possible for shareholders to remove a director from the board. [The fund] supports majority elections of directors.

In a variant of majority elections for directors, directors who do not win a majority of shareholders' votes must submit their resignations to the board, which then decides whether or not to accept the resignations. Director resignation policies are an improvement over plurality elections, but they still allow the directors to determine who sits on the board even if a majority of shareholders have voted to remove a director. If a majority of shareholders vote for a proposal to implement majority elections, [the fund] will not consider the adoption of director resignation policies to be an adequate substitute.

- [The fund] will vote for proposals to require that directors receive a majority of affirmative votes to be elected.
- [The fund] will vote for proposals to require boards to accept the resignations of directors who do not receive a majority of affirmative votes of shareholders.
- If a board does not accept the resignation of a director who fails to win a majority of shareholders' votes, [the fund] will vote against the entire board at the next opportunity. [The fund] will make exceptions to this guideline if the company makes a compelling case for retaining the director.

### Contested elections for directors

When an election for directors is contested, the dissident candidates usually want to make a significant change in corporate policy. In deciding how to vote in contested elections, [the fund] will assess how any policy changes advocated by the dissident candidates will affect the long-term interests of the company and its stakeholders. Dissident candidates must also be suitably qualified and independent.

- In contested elections, [the fund] will assess votes for directors case by case, using the criteria in this section and all of the other relevant sections of these guidelines.

### Definition of an independent director

Shareholders face difficulties evaluating the independence of directors. Most shareholders are not present at board meetings and rarely know directors personally. The information about the directors provided in proxy materials does not necessarily reveal how easy it is for individual directors to make decisions independent of management or without pressure from non-independent directors. Thus, shareholders must rely on less-than-ideal information from the company to assess how likely it is that a director can

make independent decisions about the company and its management.

In general, a director is independent if he or she has no material relationship with the company other than that of director and shareholder. This excludes any director who:

- is currently or has been previously employed by the corporation, an affiliate of the corporation, or a company that has been acquired by the corporation within the past 5 years. This includes companies with cross-shareholdings;
- is currently a director, employee or contractor of a competitor of the corporation, or has been in any of those positions with a competitor in the past five years;
- founded the company, individually or with others, if that person also maintains another relationship with the company, such as any of the relationships listed here;
- holds any contract, agreement or arrangement with the company that pays the director any compensation or benefits, other than the payments that person receives as a shareholder and a director (e.g. dividends and director's fees);
- receives benefits from the company or compensation as a director that is higher than the appropriate average, or is comparable to the base salaries of the highest-paid executives;
- is currently employed, or has been employed within the last five years, by the company's auditor;
- is employed by or owns a significant portion of an entity that does business with the company or has an immediate family member who does business with the company, including advisors, consultants, accountants, lawyers, banks, customers or suppliers. However, exceptions should be made for monopolies, such as utility companies, or very large companies that do business with many customers, such as very large banks;
- has, within the past five years, been an employee or owner of an entity that does business with the company, as described above;
- serves as a director on the board of a company that has an executive who serves on the board of the director's own company—a situation known as an interlocking directorship;
- is an immediate family member of any of the corporation's employees;
- is indebted to the corporation or any subsidiary, except for bank directors with a residential mortgage from their

institution with the same conditions and rates provided to other customers;

- is employed by any organization that receives financial support from the company or has some other close relationship with the company;
- owns a material interest in, has extended credit to, or has an immediate family member who owns a material interest in or has extended credit to an entity over which the corporation or any executive officer of the corporation exercises significant control (significant control should be defined with reference to the contractual and governance arrangements between the corporation or executive officer and the entity);
- has provided, or has an immediate family member who has provided, any professional services to any executive officer of the corporation in the last five years;
- has any other relationship similar in scope and nature to any of the relationships listed above.; or
- has been a director for more than ten years.

Directors who hold a significant interest in the company or are affiliated with or designated by a shareholder with a significant interest may also be considered not to be independent. This includes shareholders who hold less than 50% of the company's voting power if they also have business transactions with the company or a relationship to management. The determination of these shareholders' or directors' independence will be made case by case. The determination will be based on whose interests the shareholder or director is mostly likely to represent, and on whether the director or shareholder would have any potential conflicts of interest in serving on the board.

### Independent chair of the board

The chair of the board of directors must be an independent director, as defined above, to guide the board in its responsibility for overseeing management's performance. This is a basic tenet of good corporate governance.

- [The fund] will vote against directors who are not independent if they are also chair of the board or if, upon becoming director, they would become chair of the board.
- If the chair of the board is not an independent director, [the fund] will also vote against the nominating committee.
- [The fund] will vote for proposals to require the chair of the board to be an independent director.

## Independent lead directors

Some companies whose board chairs are not independent have sought to compensate by appointing an independent lead director. However, companies with an independent director as chair perform better and pay executives less than companies where the chair is an executive of the company, even if those companies have lead directors.

The appointment of an independent lead director may be suitable as an interim step toward making the board's chair an independent director, but it is not a substitute for an independent chair. An independent lead director should serve in that position for no longer than one year before an independent chair is appointed.

- [The fund] will vote for proposals to create an independent lead director position if the position exists for no longer than one year.

## Key board committees

All boards should have committees responsible for the audit, for compensation, and for nominating new board members. The members of these committees must all be independent directors. They should not be nominated or selected by management.

Audit committees should have at least one member with recent, relevant financial experience.

- [The fund] will vote against directors who are not independent and sit on the audit, compensation or nominating committees.

Supervisory boards often have committees. These are discussed in the section on supervisory boards.

Directors who are executive officers of other companies should not sit on the compensation committee unless those companies are privately held and very small, such as a company with no more than two or three employees.

If a company's compensation committee includes members who are not independent, [the fund] will give special scrutiny to the company's compensation plans. It may vote against the plans if it believes the committee's lack of independence is influencing the company's executive compensation.

- [The fund] will withhold votes for individual directors who sit on the compensation committee if they are executives of other companies, unless those companies are privately held and very small.

- [The fund] may vote against a compensation plan if the compensation committee includes directors who are not independent.
- Vote against the chair of the governance committee when a share structure has multiple classes of shares with unequal voting rights.
- Vote against all audit committee members when auditor ratification is not subject to a vote or when audit fees exceed the limit set in these guidelines (see page 17).
- Vote against all nominating committee members when one gender represents less than 30% of directors.
- At Canadian and US issuers, vote against the chair of the nominating committee when the board does not obviously include any director with a diverse racial or ethnic origin.
- Vote against the nominating committee if disclosure on board member diversity is inadequate.
- Vote against election of the remuneration committee members if there is no advisory vote on executive compensation and the compensation plan does not meet the SHARE voting guidelines for executive compensation plans.

## Term limits for directors

Term limits for directors are intended to protect boards' independence by removing directors whose independence may be compromised by relationships with management they have developed during a long tenure. However, this is an arbitrary way to assess directors' independence. Term limits may remove good, experienced directors solely because of their length of service, and inhibit a long-term view of a company's performance.<sup>2</sup> [The fund] prefers boards that have a mix of newer and long-serving directors.

- In general, vote against term limits for directors.

## Directors' ability to devote sufficient time and energy: Attendance and other commitments

Directors cannot fulfill their duties adequately if they do not attend meetings of the board and the committees of which they are members. [The fund] will vote against directors who miss 25% or more of these meetings, unless the company provides a good explanation for their absences.

- [The fund] will withhold votes for directors who are executives of a public company and serve on more than one other board. [The fund] will withhold votes for other directors who serve on more than five other boards.

- Withhold vote for a director who is the chairperson of a public company and serves on more than two other boards.
- [The fund] will withhold votes for existing directors if they have missed 25% or more of the board's meetings and committee meetings unless extenuating circumstances are set out in the proxy materials.
- [The fund] will vote for proposals to require companies to disclose directors' attendance.

### Diversity on boards of directors

To foster the long-term success of corporations, boards should recruit directors with diverse backgrounds.<sup>3</sup> Diversity should be defined broadly and can include age, professional experience, gender, race, Indigenous heritage, linguistic and cultural background, sexual orientation/identification, and disability.<sup>4</sup>

While legal and regulatory requirements related to board and employee diversity vary by jurisdiction, [the fund] expects companies to, at minimum, develop and disclose an appropriate diversity policy or explain why a policy is not appropriate to their situation.

There is no one-size-fits-all diversity policy, but not all policies are equally acceptable. Good policies are those that, if implemented, will result in a more diverse board within a specific, reasonable period. The target for gender diversity on the board should be at least 30% women directors. The target for representation of Black, Indigenous and People of colour ("BIPOC") representation on boards of directors in Canada and the United States should be 20% of the board. If a board is made up of only one gender or has no members of under-represented groups, including Indigenous peoples, an acceptable diversity policy should also acknowledge that the board needs greater diversity and explain the specific steps the board is taking to achieve it. This excludes policies to select nominees without regard to diversity, and those that reject arguments in favour of greater diversity on corporate boards.

- Vote for reasonable proposals promoting greater diversity on boards of directors.

### Employee representation on the board of directors

Within companies, shareholder primacy is being questioned. This has resulted in the commitment of 181 executives who are members of the Business Roundtable (a group of CEOs of large American companies) to run their companies for the benefit of all stakeholders. A prominent category

of stakeholders are employees, often coined their "most valuable asset" by issuers. Several European countries (Germany, Netherlands, Sweden among others) include workers representatives on their boards. A board structure with workers representative bears several advantages including: better understanding between management and other employees, higher sense of belonging as employees feel more involved in decision making, improved business performance overall.

- Vote for proposals to consider including worker representation on the board of directors.

### Classified boards/staggered terms for directors

On a classified or staggered board, directors are elected for a term longer than one year, and their terms are staggered so that only a portion of the directors come up for election each year. [The fund] opposes classified boards because they reduce corporate accountability to shareholders and make it unnecessarily difficult to change control of a board.

- [The fund] will vote against proposals to adopt a classified board of directors.
- [The fund] will vote for proposals to eliminate classified boards and institute annual elections of all directors.

If a board is classified, any new directors must be presented to the shareholders for election at the next shareholders' meeting, regardless of the expected length of their terms.

If a new director is appointed to a classified board and is not up for election at the next shareholders' meeting, [the fund] will vote against the nominating committee.

### Size of boards of directors

A board needs enough directors to maintain diversity in opinion and expertise, but not so many that the board becomes unwieldy. In general, a good size for a board is 5 to 15 directors. It is rare for a board to function well with more than 17 directors. However, the appropriate number of directors will vary with the size and nature of the corporation. [The fund] prefers boards with odd numbers of directors, because they are less likely to have tied votes.

Fixing the number of directors can limit the flexibility companies may need to alter the size of their boards should they need to add independent directors or improve the diversity of their boards. Proposals to increase or decrease the number of directors will be given careful consideration.

- [The fund] will vote against proposals to fix the number of directors at fewer than 5 or more than 17.

- [The fund] will consider voting for proposals to fix the number of directors at fewer than five if the board does not have the usual full range of responsibilities of a public company board.
- [The fund] will vote against proposals to fix or set the number of directors if less than two-thirds of the board's directors are independent.
- [The fund] will vote against proposals to fix or set the number of directors if none of the directors are women and the company does not have an adequate diversity policy.

### Director compensation

Companies must compensate their directors adequately for the time and work required to fulfill their responsibilities. However, directors are in the awkward position of having to establish their own compensation. The potential conflicts that this presents can be alleviated to some extent by requiring all compensation packages for directors to be fully disclosed and subject to shareholders' approval.

Director compensation must be structured in a way that will preserve the independence of the board. Directors' compensation plans should be separate from executive compensation plans. Directors' compensation should not be so generous that it is comparable to executives' salaries, because that creates a relationship between the company and the director that may interfere with the director's independence.

The same guidelines for the compensation of boards of directors can be applied to the compensation of supervisory boards, except that supervisory board members who are employee representatives are not subject to the same requirements for share ownership as directors.

- [The fund] will support proposals to require directors' compensation packages to be subject to shareholder approval.
- [The fund] will vote against director compensation if the amounts or details of the compensation are not disclosed to shareholders adequately or in a timely way.
- [The fund] will vote against compensation arrangements that include directors and executives in the same plan.
- [The fund] will vote against director compensation if the fees for any director are as high as or higher than the named executives' salaries, or if the directors' fees are higher than average for similar companies in the same jurisdiction.

### *Directors' share-based compensation*

The board of directors, as representatives of the shareholders of a corporation, should own shares in the corporation for the long term. However, requiring directors to own shares has some drawbacks. Boards could lose the valuable experience and outlook of prospective directors who are not wealthy enough to make share purchases or to defer their fees to acquire shares. Directors should not be required to be shareowners before being nominated to the board, and new directors should be given a reasonable amount of time to acquire the shares without undue pressure to invest large amounts in the company.

Share-based compensation for directors can support their ownership of shares, but it must align directors' interests with those of other shareholders. These plans are subject to the same guidelines about expiry, dilution, and so forth as compensation plans for management.

Directors should not be granted stock options. Stock options only have value when the exercise price rises above the grant price, which tends to focus option holders' attention on short-term fluctuations in share price. Directors need to focus instead on the long-term interests of shareholders. Stock options also do not require directors to have capital at risk.

- [The fund] will vote against stock option plans that are for or include non-management directors.
- [The fund] will vote against amendments to directors' share-based compensation plans that would allow those plans to be established, renewed, or changed without shareholder approval.
- [The fund] will vote case by case on proposals to require directors to own shares in the company, taking into consideration the terms of the requirement and how difficult the requirement will make it for nominees who are not wealthy to serve as directors.

### Retirement, benefits, severance pay, or incentive pay for directors and statutory auditors

[The fund] believes that retirement or other benefits are not appropriate for directors because they increase directors' financial reliance on the corporation, which may compromise director independence. Severance and incentive pay also undermine director independence for the same reasons.

If directors are also employed by the corporation, they may receive pensions for their employment but not for their service as directors.

This guideline also applies to statutory auditors.

- [The fund] will vote against proposals to provide retirement benefits, other benefits, bonuses, or severance pay to directors and statutory auditors.

### Disclosure of directors' compensation

Details of directors' compensation packages, including an estimate of the value of directors' share-based compensation and all other aspects of their compensation, should be disclosed to shareholders so that shareholders can cast informed votes on directors' compensation arrangements. This includes disclosing the compensation paid to individual directors, members of supervisory boards, and statutory auditors.

- [The fund] will vote for proposals to disclose to shareholders all compensation paid to directors, including the value of share-based compensation.
- [The fund] will vote against directors' compensation if that compensation is not disclosed to shareholders in sufficient detail for shareholders to understand fully what the company is paying directors for their services.

### Statutory auditors

In some jurisdictions, a board of statutory auditors is responsible for ensuring that the company's actions comply with all applicable laws. In practice, the role of statutory auditors may be ceremonial, although they are officially responsible for reviewing the work of the companies' outside auditor. All statutory auditors must be independent to carry out their responsibilities without potential conflicts of interest.

Companies incorporated in Brazil have a structure like a board of statutory auditors, called a fiscal board or fiscal council, that has oversight responsibilities similar to those of statutory auditors. Brazilian corporate law requires that members of fiscal councils be independent of management, must not also serve as directors of a company, and must not be relatives of any member of management or director.

- [The fund] will vote against statutory auditors or members of a fiscal council who are not independent according to the criteria for independent directors given above.
- [The fund] will vote against statutory auditors or members of a fiscal council if there are serious questions or concerns about the company's annual audits, such as evidence that the auditor's independence has been compromised or frequent restatements of financial reports.

### Supervisory boards

Supervisory boards do not usually include members of management but may include representatives of the employees or employees' unions. The chair of the supervisory board is typically a shareholder representative. The presence of employees on the supervisory board means that these boards cannot have the degree of independence, as we have defined it, that [the fund] prefers on boards of directors.

- At companies with a supervisory board, [the fund] will vote for members of supervisory boards unless:
  - more than two members of the board are former members of the management board;
  - the candidate is a former member of the management board and is or would be the chair of a supervisory board committee;
  - the candidate has a potential conflict of interest; or
  - voting for the candidate would not, for some other reason, be in the best interests of the company.

### Committees of supervisory boards

- Supervisory boards should have audit, compensation and nominating committees. No former members of a company's management board should sit on these committees. [The fund] will vote against members of the supervisory board if they are former members of the management board and serve on these committees.

### Ratification of the acts of the board and/or auditors

Companies in some jurisdictions require shareholders' approval of the acts of their management and supervisory boards, and/or their auditors over the previous year. In most cases, this approval does not release the boards or auditors from liability. However, companies may also ask shareholders to release their boards and/or auditors from liability. The extent to which directors' and auditors' liability is limited by these votes varies with the jurisdiction. These votes require greater caution. Auditors should not be released from liability.

- [The fund] will vote against proposals to release directors from liability if the voting agent or [the fund] has reasons to be concerned about the board's actions. Examples of such reasons are evidence of illegal acts or serious mismanagement, or of failure to provide shareholders with regular, audited financial statements.

## AUDITORS AND FINANCIAL REPORTS

### Auditor independence and the appointment of auditors

Auditor independence is vital to shareholders. A company's annual financial statement is usually the only independently verified information shareholders have about the company's performance and financial condition. Shareholders must be confident that they can rely on this information and that the independence of the auditors who reviewed the information has not been compromised.

From time to time, companies hire their outside auditors to provide them with tax advice or other services. [The fund] believes that hiring the outside auditor to perform other work has the potential to compromise the independence of those auditors. [The fund] strongly prefers auditors that do not performed services for a corporation other than the annual audit.

- [The fund] will vote for proposals to prevent the outside auditor from doing any work for the company other than the annual audit, unless the company makes a compelling case that the number of accounting firms it can work with is too limited for this to be feasible.
- [The fund] will vote against auditors if more than 25% of the fees paid to the auditors in the previous year were for services other than the annual audit.
- [The fund] will vote to approve payment of the auditor's fees when this requires a separate vote from the approval of the audit firm unless there is a reason to question the auditor's independence.

### Disclosure of audit fees

Companies should disclose all of their relationships with their auditors and all fees paid to their auditors. The fees for the audit and any non-audit services should be clearly identified. [The fund] considers fees for tax services to be non-audit services.

- [The fund] will vote against auditors if the company does not disclose the fees, it paid its auditor for the annual audit, audit-related services, and non-audit services in the previous year.
- [The fund] will vote for proposals to require companies to disclose the fees paid its auditor for the audit and for non-audit services.

### Rotation of auditors

Companies that use the same accounting firm and audit partner to conduct their audits for long periods of time run the risk of developing a close relationship that can compromise the independence of their annual audit. At a minimum, companies should change their audit partner every seven years, regardless of whether they are required to do so by law.

- [The fund] will vote against the auditors if the company has kept the same audit partner for more than seven years.
- [The fund] will vote for proposals that ask the company to change audit partners every seven years unless local regulations require the audit partner to change more frequently. [The fund] will assess proposals for a greater or lesser period case by case.
- [The fund] will vote for proposals that ask companies to disclose to shareholders how long their audit partner has served in that capacity.
- [The fund] prefers that companies rotate their audit firms every six to ten years.
- [The fund] will vote for proposals that ask the company to change audit firms every ten years. Proposals for a greater or lesser period case by case.
- If companies are not required by law to change audit partners at least every seven years, and if the same accounting firm has been the company's auditor for more than 10 years, [the fund] will vote against the auditor.

### Appointment of the auditor and financial restatements

A company's management is responsible for the accuracy of its financial statements and the quality of its internal financial controls, but the external auditor has some responsibility for detecting errors, fraud, or illegal acts in the process of forming its opinion of the company's financial statements and controls. If a company has had multiple financial restatements or has engaged in financial misdeeds that the auditor did not report on, [the fund] may vote against the appointment of that audit firm. The decision to vote against an audit firm for this reason will be made case by case, depending on the severity of the company's misconduct and the likelihood that the audit firm would have detected it.

- If a company has a history of frequent financial restatements, or if it has engaged in financial misconduct (such as back-dating stock options or misrepresenting its earnings) and the auditor has repeatedly missed this behaviour in its reports, [the fund] may vote against the audit firm.

# ACCOUNTABILITY TO SHAREHOLDERS

## REPORTS

Approval of company reports Proposals to approve the company's reports are routine matters at companies outside North America. The reports for which approval is sought must be available to shareholders well before the shareholders' meeting.

All publicly traded companies should provide their shareholders with complete, audited financial reports at least annually, even if this is not required by law.

- [The fund] will vote for proposals to approve financial or directors' reports only if the reports are audited and available to all shareholders before the shareholders' meeting, and if [the fund] has no reason to be concerned about the quality of the reports or the independence of the auditor.
- If a company does not provide shareholders with complete, annual, audited financial reports, [the fund] will vote against the auditors and/or proposals to ratify the acts of the board.

### Reports on social and environmental issues

Corporations have a responsibility to disclose to their shareholders the potential liabilities of their operations, including the risks associated with social and environmental aspects of their operations. This disclosure may be included in sustainability reports with other information on the company's social and environmental performance. [The fund] recommends the Global Reporting Initiative guidelines for creating sustainability reports.<sup>5</sup> Companies may also integrate information on their social and environmental performance into their annual reports.

- [The fund] will vote for proposals to provide shareholders with sustainability reports.

- [The fund] will vote for proposals for companies to issue integrated sustainability and financial reports, as long as the integrated reports can be understood and provide as much information as separate sustainability and financial reports would provide.
- [The fund] will vote for proposals that ask companies to report to shareholders using the Global Reporting Initiative Guidelines, the Sustainability Accounting Standards Board standards, or the Task Force on Climate-Related Financial Disclosures framework.

Companies are often asked to report on specific environmental or social issues, including the risks associated with specific operations, conditions, or practices and/or plans to mitigate those risks.

- [The fund] will vote for proposals to provide shareholders with reports related to specific social and environmental aspects of their operations, including related risks and efforts to mitigate those risks, provided the information is not already easily accessible to shareholders, does not require companies to disclose confidential or proprietary information, and can be provided at a reasonable cost.
- [The fund] will vote for proposals that ask companies to report on how they will respond to the results of previous shareholders' votes, such as large percentages of votes against directors or executive compensation plans.

### Financial reports and climate change

Climate change has become a significant, material risk for businesses of all kinds. It also creates new business opportunities in a new economy based on low carbon emissions. The Taskforce on Climate-Related Financial Disclosures (TCFD) recommends that companies include the value of these climate-related costs, risks and opportunities



in their annual financial reports. The Taskforce also provides guidance for implementing their recommendations.<sup>6</sup>

- Vote for proposals asking companies to implement the TCFD's recommendations in their annual financial reports.

## PROTECTION OF SHAREHOLDERS RIGHTS AND INTERESTS

### Exclusive forum bylaws

[The fund] opposes exclusive forum bylaws, which restrict where shareholders can sue a company. Exclusive forum bylaws deprive investors of the right to choose the court in which to sue a company without demonstrating a need for such a restriction.

- [The fund] will vote against proposals to limit the jurisdictions where shareholders can file suit against the company.
- [The fund] will vote for proposals to remove exclusive forum provisions from a company's bylaws or articles.

### Shareholder class actions

Shareholder class action lawsuits can be a legitimate method of recuperating losses from management negligence, misrepresentation, or malfeasance. Companies should not restrict shareholders use of class action lawsuits or otherwise deprive investors of this means to hold management accountable for unacceptable behaviour.

- [The fund] will vote against proposals to impose mandatory arbitration to resolve shareholder claims or otherwise restrict shareholder access to class action remedies where such actions are permitted by law.

### Supermajority vote requirements

Supermajority requirements require the vote of more than a simple majority to approve a decision or transaction. [The fund] generally opposes supermajority requirements because they are often used to prevent beneficial changes to a company.

[The fund] will vote against supermajority requirements and vote for proposals to eliminate them, unless there is a compelling reason not to do so.

### Omnibus or linked proposals

Omnibus proposals combine two or more issues into a single proposal, which is presented to shareholders for a yes-or-no vote, instead of allowing shareholders to vote on each issue separately. Examples are combining a group of bylaw

changes or several types of stock-based compensation for executives into a single proposal that shareholders can only vote for or against.

- [The fund] will vote against omnibus proposals if it is opposed to any of the issues in the proposal.
- [The fund] will vote for proposals to prohibit the use of omnibus or linked proposals.

### Confidential voting

Proxy voting typically is not done by secret ballot. This allows management to contact dissenting voters and urge them to change their votes. [The fund] believes that the proxy voting process should be confidential, impartial, and free from coercion.

- [The fund] will vote for proposals to adopt confidential proxy voting.

### Related-party transactions

Companies in some markets ask their shareholders to approve related-party transactions, in which the company engages in business transactions with a company or organization that has ties to its directors or executives. These transactions create opportunities for self-interested deals and conflicts of interest, which can compromise the board's independence or the perceived integrity of the company.

- [The fund] will vote case by case on proposals to approve related-party transactions with companies or organizations that have ties to the directors or executives. [The fund] will only approve these proposals if the company's access to suppliers or service providers is limited, the company fully discloses the potential conflicts of interest, and it has a procedure in place to protect itself from those potential conflicts.

### Quorum requirements for shareholders' meetings

The appropriate quorum size for a shareholders' meeting depends on how widely held the company is, but no company should have a quorum of less than 25%. [The fund] encourages companies with dominant shareholders to set higher quorum requirements.

Companies should not set higher quorum requirements for meetings in which there may be a vote on an issue that the board or management opposes. For example, the company should not set a higher quorum threshold for a meeting at which shareholders are seeking to replace a director.

- [The fund] will vote against proposals that would set the quorum requirement at less than 25% of voting shares.

- [The fund] will vote against proposals that would set a higher quorum requirement for meetings at which proposals will be made that are opposed by the board or management.

### Shareholder-called meetings

Shareholders have a right to call special meetings. If shareholders are required to own a certain percentage of shares before they can call a meeting, the percentage required should be one that shareholders could reasonably own given the size of the company.

- [The fund] will vote against proposals to limit or deny shareholders' right to call special meetings.
- [The fund] will vote for proposals to allow shareholders to call special meetings. If an ownership requirement is set, it should be reasonable for the size of the company.

### Shareholder proposals

(See also "Voting for directors," page 8)

Shareholders should be permitted to bring proposals to the annual meeting. These proposals should be included on the proxy ballot, and proponents should be given adequate space in the proxy circular to explain the proposal. The board should implement any shareholder proposal that is approved by a majority of the shareholders.

- [The fund] will vote for proposals to allow shareholders to bring proposals to the annual meeting where they are not permitted to do so.
- [The fund] will withhold votes from directors who fail to implement shareholder proposals that win majority approval.

### Shareholder action by written consent

Companies and/or shareholders in some jurisdictions are allowed to seek the written consent of shareholders to take an action without holding a shareholder meeting or proxy vote.

Some companies seek to eliminate or restrict shareholders' right to act by written consent to prevent a takeover of the company. However, as with other takeover defences, this often protects management at the expense of shareholders.

Action by written consent can be used at companies with a controlling shareholder to take action without the input of minority shareholders.

- [The fund] will vote against proposals to limit or deny shareholders' rights to take action by written consent,

unless the company has a shareholder who controls more than 50% of the voting rights.

- [The fund] will vote for proposals to restore shareholders' right to take action by written consent, unless the company has a shareholder who controls more than 50% of the voting rights

### Shareholders' meetings

Participation in shareholders' meetings is a basic right of shareholders. All shareholders should be given timely and sufficient information about the date, location, and agenda of shareholders' meetings and about the issues to be decided at the meetings. All shareholders should have adequate time to consider and vote on the issues.

- [The fund] will vote against proposals to shorten the notice period for shareholders' meetings if the period would be less than 21 days.
- [The fund] will vote against proposals if the company does not make sufficient information about those proposals readily available to shareholders before the meeting.

Some companies propose to hold their shareholders' meetings entirely by electronic means, without any shareholders being physically present. In order to be acceptable, these "virtual" meetings must give shareholders same opportunities to participate as if they were physically present.

- [The fund] will vote against proposals to hold shareholders' meetings entirely by electronic means, unless those electronic meetings give shareholders same opportunities to participate, including asking questions and engaging in dialogue, as if they were physically present.
- If a company adopts virtual shareholders' meetings without shareholders' approval, and if the virtual meetings do not give shareholders the same opportunities for participation as if they were physically present, [the fund] will vote against the entire board.

### Shareholders' voting rights

(See also "Unequal voting rights" page 20)

Companies in some jurisdictions are permitted to change shareholders' voting rights under certain circumstances. [The fund] believes that voting rights are an essential part of owning shares in a company and that the voting rights of shareholders should not be altered. [The fund] will vote against a company's efforts to change or limit shareholders' voting rights whenever it has an opportunity to do so.

- [The fund] will vote against proposals that would limit or change shareholders' rights to vote their shares.

- [The fund] will vote for proposals to protect shareholders' voting rights.

Some companies allow matters at shareholders' meetings to be decided by a show of hands, instead of a ballot. This procedure ignores the votes of any shareholders who are not present at the meeting - which is likely to be the majority of shareholders. [The fund] sees this practice as a violation of shareholders' basic voting rights.

- [The fund] will vote against the nominating committee of any company that decides matters at its shareholders' meetings by a show of hands instead of a ballot.

### Shareholder nominations for director

Shareholders should have the right to nominate directors provided that the nominees are well-qualified and prepared to act in the interests of all shareholders.

To nominate directors, a shareholder or group of shareholders should be required to have a meaningful stake in the company, but not so many as to be prohibitive for most shareholders. The exact proportion will depend on the size of the company. For mid-sized companies, between 3% and 5% of ordinary shares is a reasonable amount.

To prevent a shareholder from taking over a company by taking over its board, companies may restrict the number of directors shareholders may nominate. Shareholders should be permitted to nominate no less than one-fourth of the board seats.

Shareholders who nominate a candidate for director should provide the same information and same amount of information about their candidate's qualifications, independence, and potential conflicts of interest as companies provide for their nominees. Shareholders' nominations should be provided to the company in time to include candidates' information in the company's proxy information circular and on the proxy ballot. All nominees should be included and given equal treatment in companies' proxy materials.

- [The fund] will vote for proposals to allow shareholders to nominate directors if they include an ownership threshold that is reasonable given the number of shares outstanding, and a requirement that nominating shareholders should provide adequate information to other shareholders about their candidate's qualifications and independence.
- [The fund] will vote for proposals to give equal treatment in proxy materials to shareholders' and board nominees for director.

### Advance notice requirements

Many companies have advance notice requirements that set out time limits for submitting director nominations to the company, and other rules for shareholders who wish to nominate directors. These requirements are acceptable if they do not unnecessarily limit shareholders' right to nominate directors.

If the notice of a meeting is published 50 days or more before the meeting date, the deadline for shareholders to submit director nominees should be no more than 30 days before the meeting. If the notice is published less than 50 days, the deadline for submitting shareholders' nominations should be no less than 10 days after the notice, or 15 days for a special meeting. Canadian companies using the "notice and access" to provide proxy materials to their shareholders electronically should have an advance notice deadline of no more than 40 days before a meeting.

There is no reason to set a maximum number of days before a meeting for shareholders to submit their nominations. If a meeting is adjourned or rescheduled, shareholders should not be required to resubmit their nominations and other information.

Advance notice requirements should not require shareholders' nominees to agree in advance to comply with all of the company's policies and guidelines, because this may restrict the directors' ability to promote meaningful changes in the company. The requirements should allow information about shareholders' nominees to be included in the company's proxy materials and appear on the company's proxy ballot.

Advance notice requirements must be approved by shareholders before being adopted.

- [The fund] will vote against the board of directors of a company that adopts advance notice requirements without the approval of shareholders.
- [The fund] will vote case by case on advance notice requirements, based on the reasonableness of those requirements. Reasons to vote against these requirements include:
  - an unreasonable time period for shareholders to notify the company of their nominations and provide the necessary information, as described above;
  - a requirement that shareholders' nominees agree in advance to comply with all of the company's policies and guidelines;

- requirements that shareholders submit information about their nominations in excess of what is required for dissident proxy circulars; and
- provisions that require shareholders to resubmit their nominations if the company adjourns or reschedules a shareholders' meeting.
- [The fund] will vote against advance notice requirements if the company does not indicate that information about shareholders' nominees will be included in the company's proxy materials and the nominees will appear on the company's proxy ballot.

### Amendments to articles of incorporation or articles of association

All major changes in a corporation should be submitted to a vote of the shareholders.

Amendments to a corporation's articles of incorporation or association are often technical or administrative matters that will not affect shareholders' interests, but they must be carefully considered because some small changes can have a significant effect on corporate governance.

When multiple amendments are combined into a single item on in the proxy ballot, it is impossible for shareholders to approve some amendments while voting against others. See the guideline "Omnibus or linked proposals," page 17.

- [The fund] will assess proposals to amend articles of incorporation or articles of association case by case, with primary consideration given to how they affect the company and its stakeholders in the long term.
- In cases where shareholders must vote on a group of amendments as one ballot item, [the fund] will vote against the entire group of amendments if it is opposed to any of the amendments.

### Approval of second or casting votes

Some companies allow the chair of the board or of a committee to cast a second vote, or "casting vote", to decide an issue if the vote is tied. [The fund] is opposed to this practice, because it gives the chair of the board or committee one vote more than other directors or shareholders.

- [The fund] will vote against any provision for a casting vote or second vote to decide tied votes at the meetings of shareholders, the board, or board committees.

### Approval of "other business"

Sometimes companies include the approval of "other business" as an item on the proxy ballot without specifying what the "other business" consists of. Approval of such items

gives the company broad discretion to act without specific shareholder approval on issues that would otherwise require their approval.

- [The fund] will vote against the approval of unspecified "other business."

### Adjournment of a meeting to solicit votes

Companies sometimes ask shareholders for their approval to adjourn a shareholders' meeting to allow the company to solicit more votes in favour of one of its proposals. [The fund] is generally opposed to adjournments for this reason. Shareholders' votes become meaningless if the company can keep soliciting votes until it gets the outcome it wants. However, there may be circumstances in which it is reasonable for the company to make this request.

- [The fund] will vote against proposals to adjourn a meeting of shareholders for the purpose of allowing the company to solicit more votes in favour of its proposals without a compelling reason.

### Allocation of profits and/or dividends

Outside of North America, many companies must have their shareholders' approval to allocate their profits between dividends, compensation for the directors and statutory auditors, and other uses.

The amount of dividend that is appropriate depends on the size, maturity, and profitability of a company. Companies that are large, mature and have consistent income should have a payout ratio of approximately 30%.

- Vote against allocation of profits or dividend when a company's proposed dividend is higher than the net earnings (negative payout ratio).
- [The fund] will vote for scrip dividends, which give shareholders shares instead of cash dividends, if shareholders have the option of receiving the dividend in cash if they choose.

### Unequal voting rights

One vote per share is a basic principle of good corporate governance. Companies with dual class share structures have a class or classes of shares with more than one vote per share. This allows some shareholders to maintain control of the corporation without holding an equivalent amount of equity, making it possible for the company to act without the support of a true majority of shareholders.

- [The fund] will vote against the creation, issuance, or continuation of common shares that carry unequal voting rights.

- Vote for proposals to adopt a reasonable "sunset" date by which the unequal voting rights will expire.
- [The fund] will vote to replace multiple-vote shares with shares that have one vote per share unless the terms of conversion are more detrimental to the interests of the holders of subordinate voting shares than continuing the dual-class structure.
- For companies with a dual-class structure [the fund] will vote for proposals for a mandatory review of the share structure and regular re-approval by holders of subordinate voting shares.
- [The fund] will vote for proposals to opt out of "loyalty share" programs that give longer-term shareholders more than one vote per share.

### Approval of the transfer or use of reserves

To cover losses, companies may use reserves to pay the dividend, or, if shareholders approve, transfer reserve funds to other accounts. Shareholders should view this practice with caution. Using reserves to pay a dividend is not necessarily harmful if it is done infrequently. Companies may also set up special reserve funds for the purpose of paying dividends that do not affect their legal reserves.

- [The fund] will vote against proposals to transfer reserve funds or use reserves to pay dividends if financial losses have made this use of reserves necessary and the losses are regular, substantial, or due to strategic problems within the company.
- [The fund] will vote against proposals to transfer reserve funds or use reserves to pay dividends if the company has also used reserves to pay dividends in each of the last two years. This does not apply to special reserve funds established to pay dividends.

### Approval of legal formalities

These proposals ask shareholders to give management the authority to complete any formalities needed to validate the decisions made at shareholder meetings.

- [The fund] will vote for proposals to approve legal formalities.

### Approval of inter-company contracts

Some companies are required to seek shareholder approval for agreements between the company and its subsidiaries to transfer assets and liabilities.

- [The fund] will vote against the approval of inter-company contracts if the terms of the contract are not disclosed in enough detail for shareholders to assess how the transactions will affect the company.
- [The fund] will vote against the approval of inter-company contracts if they involve potential conflicts of interest.

# STEWARDSHIP OF CORPORATE RESOURCES

## CAPITAL STRUCTURE

### Share issuances

(See also “Unequal voting rights,” page 20)

Companies need some flexibility to issue shares in order to manage their share capital. However, share issuances may dilute the holdings of existing shareholders. [The fund] will vote against share issuances that are too large or too frequent.

Companies outside of North America often issue shares with pre-emptive rights, which allow shareholders to share proportionally in any new issuances of shares in the same class as the shares already own. Pre-emptive rights make share issuances less dilutive for existing shareholders.

Companies may issue new shares for general purposes, or for a specific use. Share issuances for general purposes may increase the number of shares by no more than 50% if the issuance includes pre-emptive rights, or 20% if the issuance is without pre-emptive rights.

If a company issues new shares for a specific purpose, the purpose should be disclosed to shareholders. The purpose should be a good, specific reason, such as a stock split.

Share issuances can be structured in a way that allows them to be used as a takeover defence without allowing shareholders to vote on the offer to acquire the company. [The fund] opposes these share issuances.

[The fund] will oppose issuances of shares at a price below their current market price, unless the issuance is being proposed to allow a company to raise capital quickly and inexpensively. In these cases, [the fund] will support issuances of discounted shares if the shares are

issued with pre-emptive rights and the issuance is open to all shareholders. It will oppose any other issuances of discounted shares.

- [The fund] will vote for proposals to issue shares with pre-emptive rights if the potential aggregate dilution is 50% or less, or if the company provides a sound business reason for the issuance.
- [The fund] will vote for proposals to issue shares without pre-emptive rights if the dilution is less than 20%, or if the company provides an acceptable business case for issuing additional shares.
- [The fund] will vote against proposals to issue shares where the number of shares to be issued is not specified or is unlimited.
- [The fund] will vote against proposals to issue shares if the shares will be issued at a price that is less than the shares' market price at the time of issue, unless the shares have pre-emptive rights and the issuance is open to all shareholders.
- [The fund] will vote against share issuances that could be used as a takeover defence.

[The fund] may also vote against share issuance proposals if doing so is warranted by the reasons given for the requests

### Issuances of blank-cheque preferred shares

Blank-cheque preferred shares give the board of directors broad discretion to determine the number, dividend, conversion, and other rights of preferred shares. [The fund] opposes the issuance of blank-cheque preferred shares because they give directors complete discretion over the size and conditions of the issuance and because they can be

used to thwart a takeover bid without presenting the bid to shareholders.

- [The fund] will vote against the authorization of blank-cheque preferred shares.

### Share buybacks or repurchases

Share repurchases tend to benefit shareholders in the short term, but they can be detrimental to companies in the long term. Share buybacks allow shareholders to sell their shares back to the company at a good price and usually raise the share price, at least for a short time.

However, the lift in share price that share repurchases provide is not based on improvements in the underlying performance of the company. In addition, the use of surplus cash to buy back shares can add to the volatility of the share price, make executive stock options more expensive to the company or allow a company to pay greenmail. (see "Greenmail", page 26) Furthermore, if a company uses a per-share measure of executive performance, such as earnings per share, for determining executives' bonuses, share repurchases will inflate the company's per-share performance, giving executives unearned bonus.

- [The fund] will assess share buybacks case by case for their effect on the long-term performance of the company and its stakeholders.
- [The fund] will vote against proposals to repurchase shares if the company uses per-share measures of executive performance in its executive compensation plans.
- Vote against proposals to repurchase shares if the number of shares to be repurchased is more than 10% of the total shares outstanding, if the buyback premium is more than 10% above the current share price, or if the company does not specify the quantity or maximum price of shares to be repurchased.
- [The fund] will vote against proposals to amend a company's bylaws to permit the company to repurchase its own shares without shareholder approval.
- [The fund] will vote against proposals to repurchase shares if the repurchases could be made using derivatives.

### Reissue of repurchased shares

Companies may seek to reissue repurchased shares to related parties at a discount. [The fund] is opposed to this practice.

- [The fund] will vote against proposals to reissue repurchased shares to related parties unless the proposal stipulates that the shares will be reissued within a reasonable range of their market price.

Proposals to reissue shares will also be subject to the same voting guidelines as other share issuances, including limits on the percent of share capital that can be issued. See "Share Issuances," page 22.

### Stock splits and reverse stock splits

Companies usually propose to split their stock when the stock price is high and the company wants to make its shares more affordable. This usually benefits shareholders, as long as all shareholders are treated equally and the split does not result in any additional benefits to company insiders.

Reverse stock splits, or share consolidations, can be more complicated. They are usually proposed to increase the price of shares, which can indicate that a company is having problems that are driving down the value of its shares. Also, because reverse stock splits lower the number of shares a company has, they can increase executive compensation based on any financial indicator that is measured per share (such as earnings per share).

- [The fund] will decide how to vote on stock splits and reverse stock splits case by case.

### Acquisitions, mergers, and takeover protection

Mergers, acquisitions, and takeovers are common. These transactions may pay a premium to shareholders and improve a company's performance, but they often fail to improve a company's long-term profitability and have adverse effects on its stakeholders, including employees, local communities, and taxpayers. Decisions about whether to accept a merger or acquisition must be based on what will best serve the company and [the fund's] beneficiaries in the long term, not only on the price shareholders are offered for their shares.

- [The fund] will vote on acquisitions and mergers case by case, based on the overall fairness of the transaction and the long-term consequences of the deal for the company and its stakeholders.

In some cases, the companies on either side of a merger or acquisition have the same audit firm. This creates conflicts of interest for the auditor, especially if the auditor plays any role in the transaction. [The fund] will give special scrutiny to mergers or acquisitions where both companies have the same audit partner.

### Considering the effects of acquisitions and mergers

An evaluation of the broader effects of mergers and acquisitions should include the effects on all of the company's stakeholders and the environment, such as

reduced productivity due to job losses or responsibility for environmental damage. This includes implementing the International Labour Organizations recommendations for the treatment of employees in restructuring and reorganizations.<sup>7</sup>

- [The fund] will vote for proposals that ask directors to consider the effects of mergers, takeovers, or acquisitions on employees, suppliers, the surrounding communities and other stakeholders.
- [The fund] will vote on proposed acquisitions and mergers case by case, taking into consideration the long-term consequences of the proposed transactions for shareholders, employees, suppliers, local communities, and other stakeholders.

### Takeover protection

Measures designed to protect companies from takeovers must also be evaluated carefully. Takeover defences often depress the price of a company's shares and may protect the interests of directors and executives more than they protect the company or its other stakeholders. Takeover defences require special scrutiny to ensure that the company's and stakeholders' long-term interests are protected.

### Shareholders' approval of takeover defences, mergers, and acquisitions

Any action that alters the relationship between shareholders and the board, or that results in major changes in the structure or control of the corporation should be submitted to the shareholders for a vote. No company should adopt a takeover defence without approval from its shareholders, even if it is legally permitted to do so.

- [The fund] will withhold votes for or vote against all the directors of a board that adopts a takeover defence without shareholders' approval.
- [The fund] will vote for proposals to require shareholders' approval before the company adopts a takeover defence.

### Poison pill takeover defences

Poison pill takeover defences allow a company to take some action that makes it very expensive for an unwanted acquirer to buy enough shares to gain control of the company. This takeover defence can take many forms. A few of the most common are described here.

Poison pill takeover defences can serve a legitimate purpose and benefit shareholders. However, they are also easy to abuse. Adoption of a poison pill often depresses a company's share price.

### Shareholder rights plans

Shareholder rights plans are a form of poison pill takeover defence commonly used in Canada. A company with a shareholder rights plan issues stock-purchase rights to its shareholders. If a takeover offer is tendered or a potential acquirer of the company purchases a specified percentage of the shares and the company cannot negotiate a takeover arrangement with a prospective acquirer, the rights allow shareholders other than the acquirer to buy additional shares at very favourable prices. This makes the takeover much more expensive for the acquirer.

Shareholder rights plans are intended to push potential buyers of the company to negotiate with a company's board of directors, since buyers can avoid triggering the plan by doing so.

They can ensure that all shareholders are treated equally in a takeover, and they can give the board time to negotiate a better deal with the acquirer or to solicit competing bids that would maximize the value of the company's shares.

However, shareholder rights plans also have drawbacks for shareholders. They can thwart takeover attempts that would benefit shareholders, cause the price of the company's stock to drop, and protect the directors and management rather than promoting the best interests of shareholders. Plans must be designed to protect the company from detrimental takeovers, rather than protecting the interests of the board and management.

Canadian companies must submit shareholder rights plans to a vote by shareholders when the plans are adopted and seek shareholders' re-approval every three years.

- When shareholder rights plans are submitted for shareholder approval, [the fund] will assess the plans case by case. It will vote for them only when the plan ensures that shareholders will receive a fair price for their shares in a takeover and the plan will not protect management or the board at the expense of the shareholders' interests. [The fund] will vote for a plan only
  - the threshold for triggering the poison pill is at least 20% of the company's shares;
  - the plan's definition of "acquiring person" excludes anyone who strays across this threshold without intending to take over the company, such as passive institutional investors;
  - the plan's definition of beneficial ownership does not include references to voting agreements or dispositive power;



- the plan allows a bid to acquire the company that does not trigger the shareholder rights plan to go directly to the shareholders;
- partial bids are permitted with a minimum deposit requirement or with a minimum bid that conforms to the rules of the Canadian Securities Administrators;
- the bid stands for a minimum of 105 days, unless the company voluntarily reduces the bid period or accepts an alternative transaction, such as a plan of arrangement;
- if the bid period is reduced, it must not be shorter than 35 days and the company must make a public announcement;
- the bid period is no longer than 150 days. At that time the board must either announce an alternative bid or allow the original bid to go to the shareholders;
- all competing bids must remain open for the same period as the original bid. If the board of the target company reduces the bid period, it must reduce the bid period for any competing bids;
- if more than 50% of the company's shares have been tendered at the end of the bid period, or all terms and conditions of the bid have been complied with or waived, the bid must be extended for another 10 days;
- at least 50% of the outstanding securities that are subject to the bid must be tendered before the bidder can take up and pay for the shares. This also applies to partial bids;
- the offer will be considered approved if a majority of shareholders tender their shares in response to the offer or if a majority of the votes cast by independent shareholders are in favour;
- potential acquirers can continue purchasing the stock in accordance with applicable regulations during the period in which the permitted bid stands;
- if the board wants to waive or redeem the plan in order to allow the company to be acquired by means other than a takeover bid, the shareholders' prior approval is required;
- the board can waive the plan, allowing a takeover bid to be made by sending a takeover bid circular to all shareholders, if this waiver is extended to any other contemporaneous bids. In this case, all takeover bids must be made by sending a takeover bid circular to all shareholders before the expiry of the initial bid;
- the plan does not include "flip-over" provisions that allow shareholders to purchase discounted shares of an acquiring company after the takeover;
- rights can be redeemed only with shareholders' ratification;
- private placements are not exempted from the plan;
- soft lock-up agreements, in which shareholders can break the agreement to sell their shares to a competing offer, are exempted from the plan;
- the plan does not contain provisions that exempt insiders from the plan or parts of the plan;
- potential acquirers are not required to provide evidence of financing;
- the terms "beneficial ownership" and "acting jointly or in concert" are based on ownership of shares at law or in equity, not voting rights or agreements;
- the potential acquire has the right to amend the offer during the bid period;
- the plan will be resubmitted to shareholders for approval at least every three years; and
- any amendments to the plan will be submitted to shareholders for approval.

These guidelines also apply to poison pill takeover defences that are adopted to protect the tax treatment of net operating losses.

### Other variations on poison pill takeover defences

Other forms of poison pill takeover defences exist, including some issuances of shares, share subscription rights and stock warrants. All are designed to make it expensive for a prospective acquirer to buy the company without negotiating with the board of directors. Poison pill takeover defences are acceptable if they are designed to allow the board to negotiate the best possible deal for the company. However, the plans require scrutiny to be sure they benefit the company's stakeholders and not just management or the directors. As with all other takeover defences, they should not be adopted without shareholder approval.

- [The fund] will vote against the issuance of new share subscription rights or stock warrants when they could or will be used as takeover defences.
- [The fund] will vote on other poison pill takeover defences case by case. It will vote against plans that
  - allow the board to reject, without shareholder input, offers to acquire the company that do not trigger the plan;
  - are likely to discourage takeovers that could benefit the company; or

- do not require the board to give equal treatment to all offers that comply with the rules of the plan.

### Other takeover defences

There are other, less-common types of takeover defences. These include crown jewel defences, in which the target company sells its most valuable assets to a friendly third party to make the company less attractive as a takeover target. They can also include private or targeted share placements that make a large block of the target company's shares unavailable to the would-be acquirer.

- [The fund] will assess votes on other takeover defences individually, based on how they will affect the company and its stakeholders in the long term.

### Opting out of takeover laws (United States)

In the United States, some states have laws that protect corporations from hostile takeovers. These laws often include provisions that allow corporations to opt out of their protections. Takeover-protection laws may prohibit prospective buyers from making well-financed bids for a company, or limit directors' fiduciary obligations to shareholders.

- [The fund] will vote for proposals to opt out of takeover-protection laws.

### Reincorporation

Companies may reincorporate in a different jurisdiction for legitimate business reasons, but also as a takeover defence or to limit the directors' liability. [The fund] will assess votes on reincorporation case by case.

- [The fund] will vote for reincorporation proposals when management can demonstrate that there are legitimate financial or business reasons for the move.
- [The fund] will vote against reincorporation if it is being used as a takeover defence, to limit director liability, or if shareholders' rights would be diminished as a result.

Companies may also use reincorporation as a way to shift their profits to low-tax or tax-free jurisdictions. Shareholders have an opportunity to vote on this issue when companies reincorporate in a new jurisdiction to avoid paying taxes or to minimize the amount of tax they pay. Sometimes these changes in jurisdiction are part of a merger or acquisition.

- [The fund] will vote against proposals to reincorporate, including mergers or acquisitions, if it is apparent that the company is reincorporating to avoid taxes, unless there is a compelling reason to vote for it.
- [The fund] will vote for proposals that ask companies to comply with policies or guidelines on tax avoidance and base erosion promoted by the OECD.

### Greenmail

A company pays greenmail when it buys shares held by a would-be acquirer at a price above the market price, usually in exchange for the would-be acquirer's agreement to end a takeover attempt.

Greenmail decreases the value of the company's stock. It denies shareholder the preferred price for their shares and the opportunity to decide whether the prospective takeover is in their best interests.

- [The fund] will vote for anti-greenmail proposals.
- If shareholders have the opportunity to vote on a greenmail payment, [the fund] will vote against it.
- If greenmail is paid and no vote is offered on the greenmail payment, [the fund] will withhold votes from the directors who approved it. (See "Voting for directors," page 8)

# RELATIONSHIPS WITH EMPLOYEES

## HUMAN CAPITAL AS AN ASSET

Most company assets are intangible. Their "human capital", their employees, are often their biggest intangible assets. As the US Securities Exchange Commission's Investor Advisory Committee notes,

Research has found that high quality HCM [human capital management] practices correlate with lower employee turnover, higher productivity, and better corporate financial performance, producing a considerable and sustained alpha over time. The value-relevance of HCM metrics is consistently demonstrated in financial research. A meta-review was conducted in 2015 by Harvard researchers of 92 studies that measured performance using metrics of value to investors, such as total shareholder return, return on assets, return on capital, profitability, and Tobin's Q. The review found positive relationships in most studies between financial performance, however measured, and disclosed training programs or HR policies on such topics as employee participation and pay for performance.<sup>8</sup>

Effective management of human capital is an essential part of a company's competitiveness, but its value is usually not clearly reflected in current financial or corporate reporting. Investors need adequate disclosure of companies' human resources policies, practices, and outcomes to better assess the effect of the company's human capital management on value creation. This includes a better understanding of executive and general employee compensation, and of discrimination, health and safety, and labour rights.

## EXECUTIVE COMPENSATION

Executive compensation is a controversial area of corporate governance. [The fund] does not intend to design executive compensation plans; this is the job of independent compensation committees. However, [the fund] intends to give executive compensation at all companies close scrutiny.

### Omnibus compensation plans

Elements of a compensation plan should be voted on individually. An omnibus plan combines two or more elements in a single ballot item. The use of omnibus plans is poor governance.

- Vote against Omnibus plans if any part of the plan is contrary to the SHARE executive compensation guidelines.

### Executive compensation and income inequality

The growing disparity between the incomes of the wealthiest segment of the population and the majority of working people is a concern for investors. Economic growth slows when the incomes of the wealthy rise and those of the lower and middle classes do not, with the potential to create greater social and political instability and risk.<sup>9</sup> The compensation of executives often places them among the wealthiest 1% of the population and contributes to rising disparities in income.

Good compensation plans recognize the value of the efforts of all a company's workers, and the importance of fairness as well as market considerations in allocating pay.

For companies in the US or Canada, [the fund] compares the total compensation paid in a year to a single executive to the average annual pay of all workers in the country where the

company is incorporated. We see executive pay that is more than 150 times the average annual pay of all workers in that country as cause for concern.

- If the total compensation of any of the executives named in the compensation report of a Canadian or US company is more than 150 times the average annual wage of that country, [the fund] will give the executive compensation special scrutiny. If the total compensation of any of the named executives is more than 200 times the average annual wage, [the fund] will vote against approving the executive compensation.
- In cases where executive compensation has been consistently excessive, vote against the compensation committee or the entire board of directors.

Companies may be asked or required to report on "vertical" pay comparisons between the compensation of their executive and non-executive employees. Companies may also be asked to set a maximum range or ratio that they will allow between the compensation of the two groups of employees.

Large disparities in pay within a company can foster a sense that the company is unfair, and that the contributions of non-executive workers are not valued. Although there is no single, optimal ratio of executives' pay to workers' pay, it is not in the best interests of any company for the gap between executive and employee compensation to be large enough to affect the company's morale or long-term performance, or to damage its reputation.<sup>10</sup>

- [The fund] will vote for proposals that ask companies to provide shareholders with a comparison of the compensation of their executive and non-executive employees, provided the reports can be produced without undue expense or revealing confidential information.
- [The fund] will vote on proposals to establish a specific ratio between executive compensation and workers' compensation case by case.

### Executive compensation and performance

[The fund] expects that most of executives' compensation will be based on their performance.

Performance goals should support the company's sustained, long-term value. This excludes goals such as stock price that may not reflect the performance of the company. It includes goals that support innovation, and qualitative goals that contribute to long-term value, such as customer satisfaction, environmental sustainability, and employee health and safety.

Goals and targets for executives' performance-based pay should be established at the beginning of the evaluation period. They should not be lowered except in very unusual circumstances, and with a full explanation for shareholders. Goals and targets that are based on the company's performance relative to the performance of other companies should list those companies and explain the basis on which they were selected for the comparison.

Companies that use measures of financial performance on a per-share basis, such as earnings per share, can artificially improve their financial results by repurchasing shares and give executives unearned compensation.

- [The fund] will vote against executive compensation plans that do not include performance-based compensation unless the company provides a well-reasoned explanation for not including performance-based pay in its executives' compensation.
- [The fund] will vote against incentive compensation that is not based primarily on performance.
- [The fund] will vote against executive compensation plans that allow incentive compensation to be paid for below-average performance.
- [The fund] will vote against executive compensation that is excessive.
- [The fund] will vote against compensation plans if the company uses per-share financial measures and the company has repurchased shares or asks for the authority to repurchase its shares.
- [The fund] will vote against compensation plans if share price is a significant measure of performance for determining the amount of compensation under the plan.
- [The fund] will vote against incentive compensation if the company lowered any executive's performance goals or measures after they were originally established, unless the company provides good reasons for the adjustment
- Vote against compensation plans that do not include measures of performance on social and environmental issues.
- [The fund] will vote for proposals to link executive compensation to well-considered measures of performance on social and environmental issues, as well as measures of financial performance.
- [The fund] will vote against incentive compensation if the performance evaluation period is less than one year for short-term bonuses or less than three years for long-term bonuses unless the company provides a sound reason for using a shorter period.

## Executive compensation during layoffs

Increasing the pay of management or paying them bonuses while laying off employees contradicts the principle that compensation should be linked to performance. If the company's performance is so weak that employees must be laid off, then it does not warrant an increase in executive compensation or benefits.

- [The fund] will vote for proposals to require the company to halt any increase in executive compensation during layoffs, including freezing executives' salaries, restricting the exercise of share-based compensation, and cancelling bonuses.
- [The fund] will vote against executives' compensation if it includes bonuses or raises in salary during a period when the company has laid off employees.

## Compensation recoupment or "clawbacks"

From time to time, companies award performance-based pay to their executives based on financial results that later must be restated or when executive misconduct later comes to light involving legal and regulatory breaches or behaviour contrary to company policy that puts the company reputation at risk. Most companies have "clawback" provisions that require executives to pay back part of their compensation to reflect the restated financial reports. These provisions should also apply to performance-based compensation awarded based on any fraudulent activity or other misconduct.

- [The fund] will vote for proposals asking executives to pay back an appropriate portion of their compensation when that compensation is based on financial information that must later be restated unless the restatement does not affect the criteria on which the compensation was based, or in the case of behaviour involving a breach of law and regulations or placing contravening company policy while putting the company's reputation at risk.
- [The fund] will vote against compensation plans that do not include clawback provisions unless clawbacks are already required by law.

## Approval of compensation committee reports and/or compensation policies

Companies that put their compensation reports or policies to a vote at the annual shareholders' meeting give shareholders a say on the form and amounts of the compensation given to executives. These votes are often referred to as "say on pay." They should be held annually.

- [The fund] will vote for proposals that ask companies to submit their compensation policies or compensation committee reports to an advisory vote of shareholders.

- [The fund] will vote against compensation policies or compensation committee reports if it has concerns about any aspect of the company's compensation plan.
- [The fund] will vote for proposals to adopt an annual shareholders' vote on executive compensation.

## Disclosure of executive compensation

Companies should describe their entire executive compensation plans clearly in the proxy circular, including all parts of the compensation for the named executives. The full value of executives' share-based compensation should be included in the proxy materials, and not just in the financial statements. If a company uses a peer group to benchmark its executive pay, it should disclose the companies that make up that peer group.

- [The fund] will vote against compensation policies or compensation committee reports if the report does not include enough information for shareholders to understand how the company determined or would determine the amounts the executives are paid. This includes the performance criteria on which incentive compensation is based.
- [The fund] will vote against plans if the company's disclosure about the performance criteria for its incentive compensation is so vague that shareholders cannot determine what measures of performance are being used to award performance-based pay.

## Share-based compensation

In principle, the inclusion of share-based compensation in executive compensation plans benefits a company's shareholders by aligning their interests with those of shareholders. However, share-based compensation can also give executives an incentive to focus on their company's share price instead of its productivity, profits, customer satisfaction, or other aspects of its performance.

Share-based compensation has also been a common source of excessive executive compensation. For these reasons, share-based compensation requires careful scrutiny from shareholders. This applies to all forms of share-based compensation, including forms that vest as cash instead of shares. The most common forms of share-based pay are discussed in the following sections.

[The fund] will consider the following aspects of share-based compensation for executives in evaluating this part of their compensation.

- [The fund] will vote against share-based compensation that has no expiry date or an expiry date of longer than five years.

- [The fund] will vote against any proposal that would allow the board to extend the expiry date of share-based compensation without shareholder approval unless the expiry date falls within a trading-blackout period and the extension is no more than a few days.
- [The fund] will vote against long-term share-based compensation plans vest in less than three years.
- [The fund] will vote against executive pay plans that include tax “gross-ups”, that is, additional amounts to cover the taxes on any part of the compensation.
- Vote against executive pay plans that include Stock Appreciation Rights (SARs) and Phantom stock.

### Dilution

[The fund] defines dilution as the number of shares available for share-based compensation plus all the share-based compensation that has been awarded but not yet exercised, divided by the total number of shares outstanding. This is sometimes called the overhang. Dilution of more than 10% is a sign that executives may be awarded too much share-based pay.

The grant rate or burn rate of a plan is the percentage of outstanding shares granted as compensation in a year. High grant rates are dilutive.

- [The fund] will vote against share-based compensation plans if the company’s total dilution from compensation is more than 10%.
- [The fund] will vote against share-based compensation if the average grant rate for the past three years is 2% or more. [The fund] may also vote against plans that grant stock options with grant rates above 1%, especially if their dilution is also above 5%.
- [The fund] will vote against share-based compensation plans with reload or automatic replenishment provisions that replace share-based awards when they are exercised. An exception to this guideline may be made if the company’s cumulative overall rate of dilution is so low that it is unlikely to exceed 10% for the duration of the plan.

### Stock options

Stock options have value only when the company’s share price rises above the price of the shares when the options were granted. As a result, stock options give executives an incentive to focus on the share price rather than on other measures of the company’s performance and best interests in the long term. Stock options also can be manipulated to increase their value above what it was when they were

issued. [The fund] does not favour the use of stock options as a form of compensation and prefers stock-based plans.

- [The fund] will vote for proposals to eliminate stock options as a form of executive compensation unless the options have performance requirements or there is a compelling reason not to eliminate them.
- [The fund] will vote against executive compensation plans that offer stock options at a price below the shares’ market price.
- [The fund] will vote against repricing stock options or reissuing “underwater” options whose market value is less than their exercise price.
- [The fund] will vote against stock option plans that do not explicitly prohibit repricing, reissuing, or exchanging underwater options.
- In general, [the fund] will vote against compensation plans if, in the past three years, the company has repriced or replaced stock options without shareholders’ approval. [The fund] will make exceptions if the plan and the directors responsible for the repricing have been replaced.
- [The fund] will vote against compensation plans if they do not have fixed dates or intervals for awards or if they do not prohibit timing awards of stock options in ways that artificially increase the value of the award.

### Share subscription rights

Share subscription rights are a form of stock option. They are sometimes issued without specifying the purpose for the options, who the recipients will be, or the strike price of the options. [The fund] is opposed to this practice because the options can be discounted or priced at a premium at the board’s discretion, and because unspecified share issuances have the potential to dilute the value of existing shareholdings.

- [The fund] will vote against the issuance of share subscription rights unless:
  - the price of the shares is specified and is comparable to the market price of the company’s shares;
  - the number of shares to be issued is specified;
  - a specific purpose is given for the shares to be issued; and
  - the recipients of the rights are identified.

Share subscription rights can also be used as a takeover defence. See “Poison pill takeover defences,” page 24.

## Company loans for stock purchases

[The fund] opposes the practice of making loans to employees to allow them to purchase shares, even if the loans are made at market rates. This practice may leave the company with uncollectible debt and inhibit the termination of employees who have outstanding loans with the company. These loans are illegal in some jurisdictions.

- [The fund] will vote against compensation plans that provide for loans to employees to exercise their stock options or make other share purchases.

## Change-in-control provisions

(See also "Severance benefits," below.)

Share-based executive compensation plans should not allow executives to receive more for their shares than other shareholders receive from a change in control. Change-in-control provisions should require control of at least 50% of the company's shares to change hands. Share-based compensation should vest only if a change of control is completed and the executive also loses his or her job with the company as a result. These are called "double-trigger plans," as opposed to "single-trigger plans," which require only a change of control for share-based awards to vest.

- [The fund] will vote against share-based compensation plans with change-in-control provisions if they allow holders of share-based compensation to receive more for their shares than other shareholders receive for their shares.
- [The fund] will vote against change-in-control provisions that are developed during a takeover fight.
- [The fund] will vote against change-in-control provisions that are triggered by changes in control of less than 50% of the company's shares, or by an event that does not involve changes in share ownership, such as changes in the board of directors.
- [The fund] will vote for proposals to require change-in-control transactions to be complete before any change-in-control provisions of compensation plans come into effect.
- [The fund] will vote against compensation plans that allow an executive's share-based compensation to vest if a change in control takes place unless the executive's employment with the company is terminated because of the change in control.

## Severance benefits

Executives often receive special severance packages, called "golden parachutes" if they lose their jobs as the result of a change in control. The purpose of golden parachutes is

to ease managers' concerns about losing their jobs in the event of a successful takeover, and thus help them to make decisions that are in the best interests of the company and its stakeholders. However, the amounts of golden parachutes can give executives an incentive to pursue changes in control of the company, regardless of the effect on other stakeholders. [The fund] does not look favourably on golden parachutes. Executives should not be unduly penalized by changes in control of a company, but they also should not benefit at the expense of other stakeholders.

- [The fund] will vote case by case on executive severance packages. We will only vote for them if the company demonstrates that the arrangements are in the long-term interests of its stakeholders, that they do not create a conflict of interest for the recipients, and that the amounts involved are reasonable.
- Vote against Severance plans that exceed two times the annual salary and the annual bonus of the executive.
- [The fund] will vote against any severance arrangements that allow executives to receive severance pay if their performance or the performance of the company has been unsatisfactory. This includes severance pay for executives who are fired or who resign in lieu of being fired.
- [The fund] will vote against any severance plan triggered by a change in control that is not contingent on a completed change in the ownership of more than 50% of the company's shares or voting rights.
- [The fund] will vote for proposals to require all severance packages for executives to be approved by shareholders.

## Compensation caps

Compensation caps are a somewhat arbitrary way to control excessive executive compensation. However, there are instances in which they may be the best means available to rein in runaway executive compensation.

- [The fund] will assess proposals for compensation caps case by case. In general, it will vote against them, unless executive compensation is excessive and there is no other effective way to limit that compensation.

## LABOUR RIGHTS

A company's employees are stakeholders in the company, and they make an essential contribution to the company's success. Companies whose employees are satisfied with their work conditions are more likely to enjoy greater customer satisfaction, higher productivity, and greater profitability.

The International Labour Organization's Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy, and the OECD's Guidelines for Multinational Enterprises spell out certain basic labour rights. Companies are encouraged to adopt these standards as a minimum commitment to labour rights in all operations and supply chains.

- [The fund] will vote for proposals that ask companies to report on their workplace practices, characteristics of their workforce, and on their efforts to improve the quality of their workplaces. This includes comparable reports on companies' supply chains.
- Vote for proposals that ask companies to establish a board committee on human capital management and workplace practices or assign responsibilities for this to an existing board committee.

### Discrimination in employment

(See "Labour practices," page 33)

Companies should comply with the International Labour Organization's standard on non-discrimination. Most countries prohibit discrimination in employment based on race, religion, national origin, ancestry, sex, age, and physical disability, and in many places, sexual orientation, or gender identity.<sup>11</sup> Many jurisdictions also require companies to report on various aspects of their diversity, including the composition of their workforce or boards of directors, and the pay of their employees by gender.

Employees should have full recourse to legal remedies to address claims related to their rights at work, including cases of sexual harassment and discrimination.

Research indicates that diversity is good for companies. Studies of workforce diversity have found that companies with more diverse workforces are more likely to have returns above the national median for their industries.<sup>12</sup>

- [The fund] will vote for proposals to improve diversity and equity in the workplace if those plans do not set arbitrary or unreasonable goals or require companies to hire people who are not well-qualified for their positions. It will assess these proposals case by case.
- [The fund] will vote for proposals to prohibit discrimination in employment, including proposals to expand or clarify anti-discrimination policies or sexual harassment policies and to report on the effects of policies that limit employees' right to seek redress.
- [The fund] will vote for proposals that ask companies to report on pay equity, including differences in pay based on gender, race or ethnicity, in their workforces.

### Workplace health and safety

In addition to the human costs, work-related injuries and illnesses are expensive for companies. The costs can include lost work time, repairs to equipment, fines, lowered productivity or morale, and increased insurance and workers' compensation premiums. Good workplace safety can give companies a competitive advantage.

For proposals regarding reports on workplace health and safety, see the earlier section "Reports on social and environmental issues" page 16.

- [The fund] will vote for proposals that ask companies to take steps to reduce their risks of workplace illness and accidents, including appointing a committee responsible for health and safety.
- [The fund] will vote for proposals to include well-considered health and safety performance criteria in setting executive compensation.

Sexual harassment is a phenomenon that affects both women and men, although women are more vulnerable. In the United States, it is estimated that at least 25% of women are victims at work, but this rate could reach 50% according to a survey of the Wall Street Journal and the BBC. The Ontario Human Rights Commission notes that "employers that do not take steps to prevent sexual harassment can face major costs in decreased productivity, low morale, increased absenteeism and health care costs, and potential legal expenses". In addition, harassment can lead to staff turnover and reduce the ability to attract and retain employees. In short, in addition to the obvious risks of reputational damage, companies associated with sexual harassment are exposed to financial, legal, and operational risks, even boycotts, and divestments, which can damage shareholder value.

- Vote for proposals requesting that the company assess the effectiveness of the company's policies on sexual harassment in the workplace.

### Employee share-ownership plans

Employee share-ownership plans give employees a stake in the profitability of their company, create an additional incentive for good performance, and align employees' interests with the interests of shareholders. Employee share-ownership plans differ from executive share-based compensation in that they are open to all or the vast majority of a company's employees.

Most of these plans offer employees the opportunity to purchase shares or stock options at a discount. Discounts on option or share prices should be appropriate for the market,



but no more than 20%, and less if the company's shares are highly diluted. These plans are subject to the same concerns about dilution as other share-based compensation plans. Shares acquired under these plans should be subject to a reasonable vesting period that will encourage employees to keep their shares but not penalize them should they need to sell the shares.

- [The fund] will vote in favour of employee share-ownership plans provided they discount options or shares by no more than 20%, include a reasonable vesting period, and conform to other relevant sections of these guidelines, such as dilution and loans for share purchases.

### International labour practices

One appeal of moving production overseas is that doing so allows corporations to take advantage of lower wages in some countries. Unfortunately, some corporations have sought an unfair competitive advantage by lowering their labour standards for overseas operations, resulting in a labour-standards race to the bottom. To ensure that consistently high standards are used in global employment practices, [the fund] encourages companies to adopt the labour standards in the OECD's Guidelines for Multinational Enterprise.<sup>13</sup>

- [The fund] will vote for proposals that ask companies to provide shareholders with independently verified reports on their progress in implementing the OECD Guidelines for Multinational Enterprise, or equivalent standards, unless this information is already easily available to shareholders.
- [The fund] encourages companies to establish a monitoring process that includes independent verification of contractors' compliance with labour and environmental standards. The best monitoring involves local, independent, respected organizations in the monitoring process, and uses incentives rather than premature termination of contracts to encourage suppliers to raise their labour and environmental standards.
- [The fund] will vote for proposals that ask companies to adopt due diligence practices, to evaluate their contractors' operations, and to use qualified, independent monitors to assess their contractors' adherence to labour and environmental standards.
  - [The fund] will vote for proposals that ask companies to adopt and comply with the labour standards of the OECD Guidelines for Multinational Enterprise, or employment standards or agreements that are consistent with those guidelines.

# RELATIONSHIPS WITH COMMUNITIES

## HUMAN RIGHTS

Violations of human rights can expose a company to liability for those abuses, even if the company tries to distance itself from them. Companies in some jurisdictions are legally responsible for human rights violations in their supply chains.

Adopting and implementing the United Nations Guiding Principles on Business and Human Rights, the OECD's Guidelines for Multinational Enterprises, and supplier codes of conduct can help companies avoid being associated with human rights abuses.

- [The fund] will vote for proposals to require companies to adopt and/or comply with international human rights standards, including the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles.
- [The fund] will vote for proposals that ask companies to consult with stakeholders on the effects of their operations on human rights, including organizations with expertise in human rights.
- [The fund] will assess proposals that ask companies to cease operations in countries with human rights abuses case by case, considering the potential for harm or benefit to the people of the country in question and the effects on the company in the long term.

Companies that operate in areas of conflict or areas with weak protections for human rights face serious risks, including harm to their personnel, the appearance of being aligned with parties to conflicts, damage to their reputations, regulatory sanctions in other jurisdictions, and possible litigation. They should adopt and implement policies, including the UN Guiding Principles cited in previous sections, and enhanced due diligence to ensure they are not contributing to violations of human rights.

- [The fund] will vote for proposals that ask companies to establish and implement policies to protect human rights and to ensure that they are, in fact, protecting those rights.
- [The fund] will vote for proposals that ask companies to monitor compliance with those policies and to provide shareholders with independently verified reports on their adherence to those policies, provided these reports are not already easily available to shareholders.

## RELATIONSHIPS WITH INDIGENOUS PEOPLES

All projects on Indigenous lands must respect the provisions of the UN Declaration on the Rights of Indigenous Peoples. This includes seeking the free, prior and informed consent of the local Indigenous communities, cultural heritage protection, and providing tangible benefits to those communities. For companies operating in Canada this includes a commitment to complying with Truth and Reconciliation Commission Call to Action #92. Indigenous communities must have a meaningful role in the decisions and management of any projects or corporate operations on their land. This may include decisions about plans for the end of a project, such as land reclamation.

Regardless of whether companies have operations on Indigenous lands, they should ensure that Indigenous people have equitable access to employment and training, and that their procurement programs include Indigenous suppliers whenever possible. Diversity policies and programs for suppliers, employees and directors should include Indigenous peoples.

- [The fund] will vote for proposals that ask or require companies to act in a manner consistent with the UN Declaration on the Rights of Indigenous Peoples in seeking the consent of Indigenous peoples and in proceeding with any operations on their lands.

- [The fund] will vote for proposals that ask or require companies to obtain free, prior and informed consent from Indigenous communities before proceeding with any operations on their territories.
- [The fund] will vote for proposals that ask or require companies to provide tangible benefits to Indigenous communities on whose territories those companies wish to operate or have projects.

Environmental issues often have a greater effect on Indigenous communities than on the non-Indigenous population. Meaningful engagement with Indigenous communities must include consulting them on environmental issues. Companies should respect Indigenous perspectives on, knowledge of, and cultural practices related to environmental matters.

- [The fund] will vote for proposals that ask or require companies to consult with Indigenous communities on environmental issues, and to respect Indigenous knowledge, perspectives and practices related to those issues.

## OBTAINING APPROVAL FROM LOCAL COMMUNITIES—SOCIAL LICENSE TO OPERATE

Companies that proceed with projects without obtaining and maintaining local support may face protests, sabotage, boycotts, negative publicity, and falling share prices. Companies that fail to obtain local support may also violate laws and/or international agreements. This includes but is not limited to agreements designed to protect the rights of Indigenous peoples, as discussed in the preceding section.

- [The fund] will vote for reasonable proposals that ask companies to commit to meaningful and ongoing consultation with local communities affected by their operations.
- [The fund] will vote for reasonable proposals that ask companies to seek the consent of local communities.

## FREEDOM OF EXPRESSION AND ELECTRONIC CENSORSHIP

Some countries use software or the records of cell phone companies and internet service providers to monitor their citizens, enforce censorship, or suppress dissent.

The right of free expression is not universally accepted. Nevertheless, the protection of basic human rights, including freedom of expression, is necessary for sound, long-term

investment. Companies that allow their products or records to be used for censorship or surveillance, or that turn a blind eye to the uses to which their products or data are put, may expose others to human rights abuses, expose themselves to liability for human rights abuses and lose their investors' confidence.

- [The fund] will vote for proposals that ask companies to adopt codes of conduct that include obligations to uphold freedom of expression and to prevent the companies' products or services from being used to violate the freedom of expression.
- [The fund] will vote for proposals that ask companies to report to shareholders on their progress in implementing these codes of conduct or in achieving compliance from their contractors, provided these reports are not already easily available to shareholders. This includes proposals that ask companies to establish board committees to examine and report on their practices and codes of conduct related to the protection of freedom of expression.

## POLITICAL CONTRIBUTIONS AND POSITIONS

Corporations sometimes represent their interests in policies and legislation that concern their business. However, we discourage companies from engaging in political activity. If companies choose to engage in political activity, they should disclose to shareholders all activities they engage in to influence public policy, including the full amounts spent, what the money was spent on, and the business reasons for engaging in these activities. This disclosure should include companies' memberships in organizations that engage in political activities on behalf of their members, and how companies will address potential conflicts between their policies and political positions they support directly or indirectly.

- [The fund] will vote for proposals to ban corporate political contributions and against proposals to make political contributions, including non-monetary contributions, unless the company can make a compelling case that the contribution is in its best interests.
- [The fund] will vote for proposals to require companies to disclose the amounts of, rationale for, and recipients of any monetary political contributions and non-monetary contributions to individuals or organizations to influence public policy, as well as company policies and oversight mechanisms related to political activity, lobbying, and trade association lobbying, provided this can be done without undue expense and that the reports are not already easily available to shareholders.

## PREDATORY LENDING

Predatory lending is the practice of making loans at high interest rates or with very high fees, and/or advertising and making loans in ways that obscure the full cost of borrowing. Predatory lending exposes corporations to uncollectible debt, litigation, and penalties from regulatory agencies. These practices pose a significant risk to the lender, the borrower, and entire economies.

- [The fund] will vote for proposals to require companies to develop and enforce policies barring predatory lending practices, and to report to shareholders on the implementation of those policies, unless such reports are already easily available to shareholders.

## MINING TAILINGS SAFETY

Poorly constructed and maintained mine tailings dam structures are a significant threat to human safety and the environment, as well as to shareholders. Following the failure of a tailings dam at a Vale mine in Brumadinho, Brazil in 2019 that led to the deaths of 270 people, a coalition of institutional investors created an initiative to address tailings dam risks. One outcome of the initiative is the creation of the Global Industry Standard of Tailings Management. Some mining companies with significant tailings dam structures have not yet committed to the Standard. Failure to make this commitment signifies a governance gap.

- Vote against the chair of the board at relevant companies that fail to confirm their intention to meet the Global Industry Standard of Tailings Management.

## DANGEROUS PRODUCTS AND PRODUCT LIABILITY

Although no responsible business would intentionally cause public harm, some products prove to be clearly or potentially dangerous.

If companies use processes or substances in their operations that have been shown to be hazardous, [the fund] encourages those companies to develop and implement plans to end the use of those processes or substances. Proposals asking companies to report on the safety of their products or operations are covered by the guideline "Reports on social and environmental issues," page 16.

- [The fund] will vote for proposals asking boards to establish a committee to examine and report on issues related to product safety, unless doing so would not benefit the company's shareholders or other stakeholders in the long term.

[The fund] will assess proposals to end the use of a process, or the production or sale of a product or substance, on a case-by-case basis. This assessment will include the potential hazards and liabilities associated with the product, substance, or process, existing or prospective regulation of the product, substance, or process and the costs of eliminating it.

# ENVIRONMENTAL RESPONSIBILITIES

Companies' environmental performance has a material effect on their profitability. Environmental damage carries material risks, such as legal liability and a damaged reputation. Sound environmental practices, on the other hand, can improve a company's financial performance and its reputation as well as reducing its environmental footprint.

Companies can manage their environmental performance by using the precautionary approach, described in greater detail in the United Nations Global Compact. The UN Global Compact also includes environmental principles that will help corporations to be environmentally responsible. [The fund] will generally support companies' efforts to implement these or comparable principles.

- [The fund] will vote for proposals that ask companies to adopt the UN Global Compact, or another set of environmental standards as long as these standards are at least as stringent as those in the UN Global Compact.
- [The fund] will vote on proposals that ask companies to improve their environmental performance case by case. This includes proposals to take specific actions to improve the company's environmental performance. In general, [the fund] will support these proposals as long as the action requested is based on sound evidence, can realistically be achieved by the company, does not hurt the company's long-term performance, and is not detrimental to the interests of its stakeholders.
- [The fund] will vote for proposals to establish a board committee to oversee environmental policy and performance or assign responsibilities for oversight of environmental policy and performance to an existing board committee.

## CLIMATE CHANGE

The consequences of climate change are material risks investors and businesses of all kinds must address. Companies are under increased pressure from their investors to reduce their greenhouse gas emissions to meet the targets of the Paris Agreement, intended to limit the increase in global temperatures to 1.5°C or 2°C above pre-industrial levels. Companies need to consider their long-term business plans and capital expenditures to adapt to a lower-carbon economy and lower future demand for fossil fuels.

Reducing greenhouse gas emissions can also benefit a company by reducing its energy use and costs, lowering its exposure to climate change risks, and positioning it to trade carbon credits.

- Vote against the chair of the board at companies that fail to adequately disclose climate-related emissions, risks, plans or targets at significant emitters based on the Transition Pathways Initiative rating of 3 or lower.
- [The fund] will vote for reasonable proposals calling for companies to improve oversight, management, and reduction of their greenhouse gas emissions. This includes setting clear performance targets aligned with the Paris Agreement's goals.
- [The fund] will vote for reasonable proposals that encourage boards and management to disclose steps they are taking to address climate-related risks.
- Abstain on proposals requesting an advisory vote on the company's climate/energy transition plans (Say on Climate).
- Vote against proposals on climate/energy transition plan if they do not include all the following criteria:

- Absolute targets for the next five years and a 5-10 year plan
- Phase out fossil fuel use and production; stop financing new projects
- Executive compensation, strategy and lobbying must be aligned with Paris Agreement goals
- Capital expenditures commitments aligned with Paris Agreement goals
- Address deforestation through cuts to harvesting and increases to reforestation
- Independent auditing of emissions
- Annual performance reporting to shareholders
- Commitment to a Just transition for workers and communities.

For reporting on the risks of climate change in financial statements, see "Financial reports and climate change", on page 16.

## HYDRAULIC FRACTURING

Hydraulic fracturing (sometimes called fracking) is a method for extracting natural gas and oil from underground shale formations by injecting a mixture of water, sand, and chemicals into the shale at high pressure.

Although energy companies claim that the process can be done safely, hydraulic fracturing has been associated with contaminated air, soil, and groundwater.

To date, most of the proposals concerning hydraulic fracturing have asked companies for reports on the risks of the procedure and on the company's efforts to mitigate those risks. Companies have also been asked to report on the chemicals used in hydraulic fracturing. These reports are covered by the guideline "Reports on environment and social issues," page 16.

- [The fund] will vote for proposals that ask companies to improve the sustainability of their hydraulic fracturing operations, provided the proposal will not be detrimental to the company or its stakeholders in the long term.
- [The fund] will vote for proposals that ask companies to disclose any litigation or similar risks they face from hydraulic fracturing or related operations.

## WATER USE MANAGEMENT

Water scarcity is a growing problem that affects business in many sectors. Companies can begin to manage water use responsibly by assessing the value of water to a business's operations, instead of focusing solely on how much it costs. As with other potential risks, businesses should disclose to their shareholders the company's exposure to water-related risks and how it manages those risks. [The fund] recommends that companies use the CDP for reporting on their use of water and related risks.

Proposals asking companies to report on their use and management of water are covered by the guideline "Reports on social and environmental issues," page 16.

- [The fund] will vote for proposals that ask companies conserve water or to improve how they manage their use of water, provided the proposal would not be detrimental to the company or its stakeholders in the long term.
- [The fund] will vote for proposals for greater disclosure of companies' potential risks related to their use of, disposal of, and effects on water, and their plans to address those risks.

## ANIMAL WELFARE

Proposals concerning animal welfare may ask companies for reports on how they treat animals in their operations, or on how their treatment of animals affects the environment and human health. Proposals may also ask companies to change the way they treat animals.

Proposals for reports on animal welfare are covered by the guideline on reports on environmental and social issues on page 16.

- [The fund] will vote case by case on proposals that ask companies to change the way they treat animals, taking into consideration the costs and benefits of making the change and the effect the proposed change will have on the company and its stakeholders in the long term.

## ENDNOTES

- <sup>1</sup> The TSX makes exceptions for contested elections, in which there is more than one candidate for a position on the board, and for controlled companies, in which a shareholder or shareholders hold a controlling number of shares.
- <sup>2</sup> "[B]oard-wide term limits may be detrimental to the board itself, the company, and the shareholders, in particular if such limits force valuable directors off the board." J. Deng, K. John, M. Ferrari, S. Bonini, "On Long-Tenured Independent Directors", *Harvard Law School Forum on Corporate Governance and Financial Regulation*, 5 June 2017, <https://corpgov.law.harvard.edu/2017/06/05/on-long-tenured-independent-directors>.
- <sup>3</sup> Companies with diverse boards and workforces are likely to have better financial results than their peers. See, for example, <https://www.mckinsey.com/business-functions/organization/our-insights/delivering-through-diversity>.
- <sup>4</sup> See, for example, the Canadian Council on Board Diversity's definition of diversity: "The Council's definition expands the traditional board definition of industry experience, management experience, functional area of expertise, education, geography and age to also include such considerations as ethnicity, gender and indigenous status."
- <sup>5</sup> See, [https://www.globalreporting.org/standards?dm\\_i=4J5,4JZIT,IXZ4Q,GVZWH,1](https://www.globalreporting.org/standards?dm_i=4J5,4JZIT,IXZ4Q,GVZWH,1).
- <sup>6</sup> See <https://www.fsb-tcfd.org/wp-content/uploads/2017/06/FINAL-2017-TCFD-Report-11052018.pdf>.
- <sup>7</sup> See, Policy 34 of the International Labour Organization *Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy*, United Nations, adopted 1977, updated and reissued 26 October 2018. [http://www.ilo.org/manila/publications/WCMS\\_647981/lang--en/index.htm](http://www.ilo.org/manila/publications/WCMS_647981/lang--en/index.htm).
- <sup>8</sup> <https://www.sec.gov/spotlight/investor-advisory-committee-2012/human-capital-disclosure-recommendation.pdf>.
- <sup>9</sup> E. Dabla-Norris, K. Kochhar, N. Suphaphiphat, F. Ricka, E. Tsounta, *Causes and Consequences of Income Inequality: A Global Perspective*, IMF Discussion Note SDN/15/13, International Monetary Fund, June 2015. [https://www.imf.org/~media/Websites/IMF/imported-full-text-pdf/external/pubs/ft/sdn/2015/\\_sdn1513.ashx](https://www.imf.org/~media/Websites/IMF/imported-full-text-pdf/external/pubs/ft/sdn/2015/_sdn1513.ashx).
- <sup>10</sup> Large disparities between the pay of the CEO and workers in a company have been found to correlate with lower profit margins and lower sales or revenue per employee in all but one sector. See, S. Block. "Income Inequality and the Intracorporate Pay Gap". Research paper. MSCI Inc., April 2016. <https://www.msci.com/www/research-paper/income-inequality-and-the/0337258305>.
- <sup>11</sup> The Canadian Human Rights Act prohibits discrimination based on race, national or ethnic origin, colour, religion, age, sex, sexual orientation, gender identity or expression, marital status, family status, genetic characteristics, disability and conviction for an offence for which a pardon has been granted or in respect of which a record suspension has been ordered. *R.S., 1985, c. H-6, s. 3; 1996, c. 14, s. 2 2012, c. 1, s. 138(E); 2017, c. 3, ss. 10, 11, c. 13, s. 2.*
- <sup>12</sup> V. Hunt, D. Layton, S. Prince. *Why Diversity Matters*. McKinsey & Company, January 2015
- <sup>13</sup> <http://mneguidelines.oecd.org/2011Employment&IndustrialRelations.pdf>.

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