

## STEWARDSHIP PRINCIPLES

Stewardship for institutional investors means fulfilling their responsibilities as fiduciaries in meeting their obligations to their beneficiaries or clients. Stewardship is intended to enhance the long-term sustainable creation of value, so companies and their investors can prosper and, in the process, benefit the market and society as a whole.

The CCGG's seven stewardship principles express what we believe are appropriate stewardship responsibilities. They are intended to help institutions investing in Canadian public equities be active and effective stewards of their investments and are directed to both asset owners and asset managers.

The principles update the CCGG's *Principles for Governance, Monitoring, Voting and Shareholder Engagement* published in 2010, which was an update to our original 2005 publication.

The principles are designed to help articulate fiduciary responsibilities. They are not intended to impose an unreasonable burden on investors. The principles are voluntary and principles-based, and CCGG will not monitor compliance. In recognition of the global nature of modern investment activity, we have designed the principles to complement, rather than supersede or conflict with, the stewardship principles or codes of other countries or other investor organizations that institutional investors may choose to follow.

### Corporate governance – a shared responsibility

CCGG advocates for the good governance of Canadian companies. Our *Building High Performance Boards* outlines best principles and guidance for corporate boards in fulfilling their responsibility to oversee management and to meet their fiduciary duty to act in the best interests of the corporation.

We recognize, however, that in the modern publicly traded corporation, corporate governance is a shared responsibility. While the board of directors oversees management, shareholders have a significant role in corporate governance in overseeing that the board fulfills its responsibilities and holding directors to account when this is not the case.

Our stewardship principles focus on the governance aspects of the shareholder's stewardship responsibilities, explaining how institutional investors can meet their obligations and enhance the value of their investments.

## Elements of stewardship

We recognize that it is not the institutional investor's role to manage the companies in which it invests.

Investor stewardship includes exercising voting rights and monitoring and engaging with companies on issues that might have an impact on the company's value. Monitoring a corporate board's oversight of strategy and risk, performance and compensation, including material environmental, social and governance factors, are all part of meaningful stewardship. We also recognize that deciding to divest from a company may be an appropriate way of carrying out stewardship obligations.

As is the case with Building High Performance Boards, the seven stewardship principles are not prescriptive – they provide guidance only. How investors implement the principles will depend on the nature of their business model and their relationships with their beneficiaries or clients. Since activities within the investment chain vary, asset owners and asset managers need to decide how best to meet the spirit of the principles in light of their specific context.

Institutional investors should, however, aim to be as transparent as practical about their stewardship activities with their beneficiaries or clients, including voting, engagement and communicating how they apply these principles, while recognizing that at times confidentiality may be crucial to achieving a positive result.

## Responsibility for third parties

Asset owners and asset managers cannot delegate their fiduciary duties or abdicate their stewardship responsibilities – they are responsible for the activities of third parties they retain.

Asset owners that delegate stewardship activities to third parties such as asset managers, investment consultants or proxy advisors, are responsible for monitoring those organizations to try to make sure they act in the best interests of beneficiaries and in accordance with the spirit of the principles. Asset managers are also responsible for monitoring third parties they retain, to try to make sure those companies are acting in the best interests of the asset managers' clients. Third parties should also follow these principles as appropriate.

## CCGG's Seven Stewardship Principles

Institutional investors are encouraged to apply the following stewardship principles:

*Principle 1* – Develop an approach to stewardship

*Principle 2* – Monitor companies

*Principle 3* – Report on voting activities

*Principle 4* – Engage with companies

*Principle 5* – Collaborate with other institutional investors

*Principle 6* – Work with policy makers

*Principle 7* – Focus on long-term sustainable value

### Principle 1 – Develop an approach to stewardship

Institutional investors should develop, implement and disclose their approach to stewardship and how they meet their stewardship responsibilities.

#### Guidance

Institutional investors should integrate stewardship into the investment process, including a procedure for voting proxies, engaging with companies, outsourcing stewardship activities, reporting to their beneficiaries or clients, managing potential conflicts of interest and aligning compensation with stewardship principles.

An institutional investor's stewardship responsibilities include engaging with the companies they invest in and monitoring the company's strategy and risk oversight (including environmental, social and governance risk in addition to financial risk), performance, governance framework and compensation.

Institutional investors cannot delegate their fiduciary duties or abdicate their stewardship oversight responsibilities. When they outsource their stewardship activities, investors should monitor the outsourced activities to make sure they are consistent with the investor's approach to stewardship. Mandates between asset owners and asset managers should set out expectations for stewardship activities carried out by the asset managers. Asset owners should monitor compliance with the mandates on a regular basis.

Institutional investors should disclose to their beneficiaries or clients, as the case may be, the internal governance structures and processes they have in place to seek to ensure that their stewardship responsibilities are being fulfilled.

They should report periodically on their stewardship activities to their beneficiaries or clients and explain how the activities are designed to protect and enhance the long-term sustainable value of the institutional investors' assets for the benefit of the beneficiaries or clients.

Institutional investors should implement mechanisms to deal with conflicts of interest within their investment activities, including how conflicts of interests are identified and managed with the objective of putting the interests of beneficiaries or clients first. The mechanisms should address situations where the interests of beneficiaries or clients diverge from each other.

Institutional investors should have structures and processes in place to seek to ensure that their compensation programs are properly aligned with the goal of enhancing the long-term sustainable value of the institutional investors' assets for the benefit of their beneficiaries or clients. Compensation programs should incorporate appropriate benchmarks, if relevant, and risk mitigation features.

## Principle 2 – Monitor companies

Institutional investors should monitor the companies in which they invest.

### Guidance

Effective monitoring of portfolio companies is an essential component of stewardship and can help institutional investor mitigate risk and enhance value for the benefit of clients or beneficiaries. Monitoring the governance of the companies in the institutional investor's portfolio is an important part of its monitoring activity.

Monitoring can include one or more of the following:

- reviewing public disclosures, including annual reports and proxy circulars
- conducting research and analysis on the company
- obtaining third party research or analysis
- sharing research and information with other investors or investor groups
- engagement, as more fully discussed below
- attending or monitoring formal shareholder meetings where appropriate and practical

Given the potential size, and in some cases the passive nature, of portfolios, investors should have a methodology for identifying companies that require further analysis and engagement. To the extent possible, investors should periodically review and consider the effectiveness of their monitoring activities and communicate the results to their beneficiaries or clients.

## Principle 3 – Report on voting activities

Institutional investors should adopt and publicly disclose their proxy voting guidelines and how they exercise voting rights.

### Guidance

Institutional investors should seek to vote all of the shares of the companies in their portfolios.

They should make informed and independent voting decisions in the best interests of beneficiaries or clients, and not automatically support management and the board. They should vote taking the particular circumstances of each company into consideration and avoid a ‘tick the box’ approach. If they use proxy advisors or other third parties to assist with their voting decisions, investors should assess the advice received and not automatically follow it. Institutional investors also should have processes in place to try to make sure votes are cast consistent with their own voting policies. Institutional investors should not borrow or lend shares for the purpose of voting.

Institutional investors should report periodically on their voting activities to their beneficiaries or clients. Reporting should disclose:

- specific instances when they will *not* vote – for example, when holdings are below a certain threshold, voting costs outweigh benefits, or clients instruct that the shares are not to be voted
- any potential conflicts of interest related to the exercise of voting rights, and how these are addressed
- their approach to stock lending and recalling lent shares for voting purposes.

## Principle 4 – Engage with companies

Institutional investors should engage with portfolio companies.

### Guidance

Institutional investors should establish an approach to engagement that includes the nature and level of concern that will prompt an engagement, and guidelines for engagement depending on the nature of the investment or size of shareholding.

Institutional investors should also thoughtfully consider with whom they should engage: independent directors, management or controlling shareholders.

The best approach will depend on the issues to be discussed. For example, an institutional investor might choose to correspond with a board or hold confidential meetings with board members if it has concerns about:

- the company's approach to governance, including the rights afforded to shareholders
- board composition and independence
- board oversight of strategy
- board oversight of risk, including material sustainability factors relating to matters such as environmental, social and governance risks
- the board's approach to executive compensation.

Engagement activities should be integrated, incorporating the expertise of the institutional investor's portfolio managers *and* its responsible investment professionals. Investors should make it clear they do not want to receive any material non-public information during the engagement, and that the disclosure of this information would require the investor's prior consent.

Institutional investors should consider how and when they might escalate engagement activities if a board is unresponsive to the concerns communicated. Escalation could include, for example:

- voting against (where legally permitted) or withholding votes from directors or voting against management say on pay resolutions
- speaking at shareholder meetings
- making public statements
- supporting or submitting shareholder proposals
- requisitioning a special shareholders meeting to address specific concerns
- nominating one or more directors by proxy access where available, or by requisitioning a special shareholders meeting or submitting a shareholder proposal
- seeking governance improvements, including through possible legal remedies.

## Principle 5 – Collaborate with other institutional investors

Institutional investors should collaborate with other institutional investors where appropriate.

### Guidance

Collaborative activity benefits both institutional investors and the companies in which they invest. It provides an opportunity for institutional investors to consider and adopt widely held principles, and helps companies understand the breadth of viewpoints on good governance practices and processes. Collaborative shareholder engagement can also be more effective than a single investor engaging with a company on its own. Accordingly, institutional investors should be prepared to collaborate directly with other investors, domestic or foreign, or indirectly by joining investor associations such as CCGG.

## Principle 6 – Work with policy makers

Institutional investors should engage with regulators and other policy makers where appropriate.

### Guidance

Institutional investors should try to make sure policymakers and regulators are considering the shareholder perspective when developing new laws and policies. Investors should also work to improve the existing regulatory environment so that shareholder rights are protected, and institutional investors are better able to carry out their stewardship obligations to their beneficiaries or clients.

Institutional investors should also consider when it is appropriate to collaborate with other institutional investors or through investor organizations like CCGG to increase the effectiveness and efficiency of engaging with policy makers.

## Principle 7 – Focus on long-term sustainable value

Institutional investors should focus on promoting the creation of long-term sustainable value.

### Guidance

Institutional investors should focus on a company's long-term success and sustainable value creation in preference to short-term considerations (understanding that beneficiaries or clients may have specific objectives and investment horizons). This focus should include understanding the company's strategy.

Institutional investors should make sure they understand the risks and opportunities associated with material sustainability factors, including environmental, social and governance issues, and integrate them into their investment and stewardship activities. Institutional investors also should be aware of systemic risks that can affect the companies in which they invest.