

**PUBLIC SECTOR PENSION INVESTMENT BOARD**

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**PROXY VOTING GUIDELINES**

**Approved by the Board of Directors on November 12, 2009**

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## **1. PUBLIC SECTOR PENSION INVESTMENT BOARD**

### **1.1 Objects**

The Public Sector Pension Investment Board (“PSP Investments”) is a Crown corporation established by Parliament pursuant to the *Public Sector Pension Investment Board Act*. The objects of PSP Investments are to:

(a) manage amounts that are transferred to it under the Canadian Forces Superannuation Act<sup>1</sup>, the Public Service Superannuation Act and the Royal Canadian Mounted Police Superannuation Act in the best interests of the contributors and beneficiaries under such Acts; and

(b) to invest its assets with a view to achieving a maximum rate of return, without undue risk of loss, having regard to the funding, policies and requirements of the pension plans (the “Plans”) established under such Acts and the ability of the Plans to meet their financial obligations.

### **1.2 Corporate Governance**

Corporate governance means the processes and structures used to direct and manage the business and affairs of companies with the objective of enhancing the value of the company. In pursuing its objects set out above, PSP Investments will give due consideration to corporate governance principles in assessing its ownership of shares in the capital of companies and, when necessary, will exercise its voting rights with a view to maximizing the value of such shareholdings.

### **1.3 Proxy Voting**

These Guidelines have been established by PSP Investments to address the areas of corporate governance with respect to which it may be requested to vote from time to time and the principles on which it will rely, at least initially, in determining a response to such requests. These Guidelines are not rigid rules. We will consider any specific circumstances on a case-by-case basis.

These Guidelines will be reviewed on an annual basis by the Governance Committee which will recommend for approval by the Board of Directors, any amendments deemed necessary.

## **2. BOARD OF DIRECTORS**

### **2.1 Independence of Boards of Directors**

A Board of Directors should have a majority of independent directors and ensure that it is able to operate independently of management. We believe that directors, who are in a

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<sup>1</sup> PSP Investments also manages the amounts that are transferred to it by the Reserve Force Pension Fund, in accordance with the Canadian Forces Superannuation Act.

position to exercise objective judgement, free of any external influence, are best positioned to successfully direct and control a company in a way that ensures the creation of long-term shareholder value.

For these purposes, “independent director” means an individual who has no direct or indirect material relationship with the company. A material relationship is a relationship which could be reasonably expected to interfere with the exercise of an individual’s independent judgement. In determining the materiality of the relationship, we will consider the stock exchange listing requirements respecting corporate governance and the requirements for disclosure of corporate governance practices under securities laws applicable to the company.

We will generally support resolutions to elect directors where the resulting Board will be constituted of a majority of independent directors.

## **2.2 Nomination and Performance Review Process**

A strong Board of Directors is made up of members with an appropriate and diverse range of competencies, knowledge and experiences to enable it to discharge effectively its duties and responsibilities.

The nominating committee should have a policy for identifying qualified candidates and proposing new nominees. The policy should take into account the skills and competencies that the Board of Directors, as a whole should possess, as well as the skills and competencies of the existing directors and of new candidates. The nominating committee should also encourage the implementation of procedures for assessing the effectiveness of the Board of Directors, the committees, their members and the contribution of the chief executive officer to the company’s results.

We will support the election of directors with the competencies, knowledge and experience to represent the best interest of all shareholders.

## **2.3 Committees**

The Board of Directors should establish a number of committees, including at least an audit, a compensation and a nominating committee. These should generally consist of at least three members and all of whom must be independent directors, as defined above. The terms of reference (charters), composition, accountability and working procedures should be well-defined and disclosed.

We will generally vote against or withhold our vote for any non-independent candidate seeking appointment to the audit committee, or in the case of the compensation or nominating committees, any non-independent candidate without adequate explanation. The company should namely disclose the steps it takes to ensure objective compensation and nominating processes.

## **2.4 Size and Effectiveness of Boards of Directors**

The Board of Directors should periodically review its own size and determine the number of members which ensures its effectiveness. We have a preference for Boards comprised of no less than five members and no more than eighteen members. This Board size is small enough to be cohesive and effective and large enough to ensure the requisite diversity of experience and skills. We will not ordinarily vote against the company's directors simply because the size of the Board does not conform to our guidelines. We will review resolutions to increase or decrease Board size on a case-by-case basis.

## **2.5 Individual Vote for Election of Directors**

We believe that shareholders should have the opportunity to vote for or against the election of each director rather than as a slate.

We will support the proposals for the election of directors individually rather than as a slate. We will not ordinarily vote against or withhold our vote from the entire slate of candidates but will do so when we have concerns about company performance, Board effectiveness and director independence.

## **2.6 Majority Vote for Election of Directors**

We will support the establishment of a majority vote standard for the election of directors. We believe that electing directors is the most fundamental right for shareholders and thus should have the opportunity to vote for or against a director candidate. However, an exception to the majority vote standard should apply in cases of contested elections, where there are more director candidates than Board seats. In these situations, the plurality voting standard remains more appropriate. Under the plurality voting standards, a director candidate is elected by receiving the highest number of votes cast even if less than a majority.

Many companies have adopted corporate governance policies requiring directors standing for election who receive more "Withhold" votes than "For" votes to submit their resignation to the Board of Directors. These policies are intended to increase the accountability of directors while maintaining a plurality voting system. These policies will be considered and may result in a vote "Against" a majority vote proposal if determined that a particular adopted policy presents a meaningful alternative.

We will not ordinarily vote against a company director's candidate simply because the company fails to meet the majority vote standard.

## **2.7 Cumulative Voting for Directors**

Cumulative voting enables a shareholder to cast all votes for a Board of Directors in favour of one candidate. It is intended to give Board representation to shareholders holding a minority interest.

We will review cumulative voting proposals on a case-by-case basis and will vote for such proposals if they ensure an independent voice on an otherwise unresponsive Board of Directors.

## **2.8 Classified or Staggered Boards**

In a classified or staggered Board, directors are typically elected in two or more classes, serving terms greater than one year.

We prefer the annual election of all directors and will generally support proposals to declassify staggered Boards.

If a proposal to adopt staggered terms for directors has been approved by the shareholders, we will generally support the directors who are standing for staggered terms in those instances in which a vote for such directors is viewed to be in the financial interests of the shareholders and otherwise in conformity with the guidelines for the election of directors.

## **2.9 Proxy Access**

In Canada, subject to sufficient requirements regarding share ownership, shareholders of companies have the right to nominate candidates for election to the Board of Directors in the company's proxy materials. In certain jurisdictions, shareholders do not have access to a company's proxy materials and must incur the cost of a proxy contest to put forward their candidates.

We will generally support proposals requesting that companies implement a procedure to allow shareholders to nominate candidates for directors in the company's proxy materials subject to sufficient requirements regarding share ownership.

## **2.10 Director Time Commitment**

We recognize that directors benefit from their exposure to other company Boards. However, directors should ensure they can manage their commitments on multiple Boards without compromising their ability to discharge effectively their duties and responsibilities.

We encourage Board of Directors to adopt and disclose guidelines in the company's proxy circular to address competing time commitments that directors are faced when directors, especially acting Chief Executive Officers, serve on multiple Boards. We may vote against or withhold our vote from a candidate seeking election to the Board of Directors of a company in situations where we believe that the candidate's commitments

on multiple Boards could compromise his or her ability to discharge effectively his or her duties and responsibilities to the company.

## **2.11 Attendance Record of Directors**

A director who commits to serve on a public company should be prepared and able to make attendance at and contribution to the Board of Directors and the Board Committees' meeting a priority.

We will vote against or withhold our vote for directors who have attended less than 75% of the meetings of the Board of Directors and the Board Committees within the past year without a valid reason for their absence.

## **2.12 Separation of Chair and Chief Executive Officer Roles**

Since the role of Chair of the Board of Directors and Chief Executive Officer (CEO) and the competencies, knowledge and experience required for them are different, they are most effectively discharged by two persons. Consequently, we believe that the Chair of the Board should be an "independent director". If such separation does not exist, we will not ordinarily vote against the company's director candidates if an independent lead director has been appointed with a role and responsibilities similar to those of a Chair of the Board of Directors. We will vote against the Chair of the Board if there is no lead director and there are continuing issues relating to corporate governance matters.

We will support proposals to separate the role of Chair of the Board of Directors and Chief Executive Officer and the appointment of an "independent director" as Chair of the Board of Directors.

## **2.13 Director Liability & Indemnification**

We will generally support proposals that limit directors' liability and provide them with a suitable indemnification, provided that the directors acted honestly and in good faith with a view to the best interests of the company and, in criminal matters, that the directors had reasonable grounds for believing that their conduct was lawful.

## **3. AUDITORS**

### **3.1 Appointment of Auditors**

We will generally support the appointment of the auditors recommended by an audit committee of the Board of Directors comprised solely of independent financially literate directors. We will review on a case-by-case basis any sudden and unanticipated proposed change to the appointment of auditors.

### **3.2 Auditors Compensation and Integrity**

We will generally not support the appointment of auditors where the level of non-audit fees earned by the auditors in the previous fiscal year is excessive or give rise to a breach of industry-accepted auditor independence standards or where the integrity of the audit has been compromised. In these circumstances, we may vote against or withhold our votes from all candidates who are up for election and who served as members of the audit committee during this time.

## **4. MANAGEMENT AND DIRECTOR COMPENSATION**

### **4.1 Compensation Review Process**

Compensation and incentives to executives and directors should be suitably structured to enhance shareholder value while rewarding performance that meets or exceeds stated objectives.

The compensation policies of a company and preferably amounts payable to the senior executives and directors should be disclosed in the proxy circular so that the shareholders can assess whether the interests of senior executives and directors are aligned with their own. The disclosure of the shareholdings of senior executives and directors is also important information for the shareholders.

### **4.2 Director Compensation**

We also believe that remuneration and fees for non-executive directors (the annual retainer and per diems for attending each Board and committee meeting) should be at a level that makes serving as a director financially worthwhile for qualified individuals. We will support director fee levels that reflect the expertise, responsibilities and time commitment expected.

We will generally support proposals that provide for a certain percentage of directors' compensation to be in the form of shares or deferred share units. We will not ordinarily vote against a slate of directors where there does not exist a practice of paying some percentage of director compensation in common shares or deferred share units.

### **4.3 Management Compensation**

Compensation packages should be sufficient to attract, retain and motivate executives of calibre, but should be linked to performance. The compensation committee should report and comment in the proxy circular on the diverse elements of the company's compensation practices, including the processes used to establish appropriate compensation packages for the senior executives, the portion and type of compensation affected by performance and the short versus long-term incentives.

We may vote against or withhold our vote from candidates who served on the compensation committee during the previous year in situations where we believe that there exists a significant misalignment between pay and performance.

#### **4.4 Equity Compensation Plans**

For the purposes of these Guidelines, Equity Compensation Plans include:

- i. Stock option plans;
- ii. Individual stock options if not granted pursuant to an equity compensation plan previously approved by the company's shareholders;
- iii. Stock appreciation rights involving issuances of shares;
- iv. Any other compensation or incentive mechanism involving the issuance or potential issuances of shares of the company; and
- v. Any other compensation or incentive mechanism which gives the right to the monetary equivalent of the increase in the value of a specified number of shares over a specified period of time without requiring any issuance, purchase or sale of shares.

We will examine Equity Compensation Plans on a case-by-case basis with a view to ensuring that the interests of the senior executives and of the shareholders are aligned. We will support Equity Compensation Plans that are properly designed to improve the competitiveness of companies. The following points guide us in deciding whether or not to support proposed Equity Compensation Plans:

*Shareholder Approval:* The terms and conditions of all Equity Compensation Plans should be approved by the shareholders before initial implementation and before any amendment takes effect.

*Price:* Equity incentives should not be issued at a discount to the current market value. We have a preference for a price formula based on the average of the share opening and closing prices on the grant date.

*Re-pricing:* Boards of Directors should not have discretion to lower the exercise price of options or other form of equity incentives already granted if the share price falls or underperforms the market.

*Expiry:* Options should not have a life of more than ten years.

*Vesting:* Equity incentives should vest over a period of three or more years. No option should be fully vested when granted. We encourage the Compensation Committee to establish vesting schedule linked to quantifiable individual and corporate performance measures.

*Performance Criteria:* The allocation and the vesting of equity incentives should be linked to quantifiable individual and corporate performance measures. This is especially important for Equity Compensation Plans above the 5% potential dilution threshold.

*Dilution:* The total potential dilution of all Equity Compensation Plans should not exceed 10% and ideally 5% of shares outstanding. The number of equity incentives granted in a given year expressed as a percentage of shares outstanding should be less than 1% per year (or 20% of the equity incentives available under the Equity Compensation Plan). The total potential dilution of “evergreen” stock option plans should not exceed 5%.

*Concentration:* No more than 20% of the available equity incentives should be allocated to any one individual in any given year.

*Director Eligibility:* Directors may be eligible participants in an Equity Compensation Plan if the terms and conditions of their participation are clearly defined and are reasonable. However, the director eligibility should not be discretionary.

*Board Discretion:* Board of Directors should not have broad discretion in setting the terms and conditions of Equity Compensation Plans. Such plans must be submitted to the shareholders for approval with adequate detail regarding their terms and conditions.

*Change of Control:* Change of control provisions in Equity Compensation Plans should not allow the automatic waiving of vesting provisions in the event of a change of control. We expect that the underlying financial performance of a company that is subject to a change of control should be a key determinant of what equity incentives, if any, should vest for participants.

#### **4.5 Employee Stock Purchase Plans**

We support employees having the opportunity to acquire shares on favourable terms in the company they work for. Employee stock purchase plans align employee interests with creating value for shareholders. We will generally approve employee stock purchase plans where the purchase price is at least 85% of fair market value and the potential dilution is less than 10%. Where their share ownership is subsidized by the existing shareholders, employees should be required to hold shares purchased for an appropriate period.

#### **4.6 Employee Loans**

Although we encourage employee share ownership, we believe that a company should not be making loans to employees to allow them to pay for equity incentives or to purchase shares.

#### **4.7 Advisory Vote on Compensation**

We will generally vote in favour of shareholders' resolutions that call for non-binding shareholder ratification of executive compensation policies. We believe that these resolutions give shareholders the opportunity to express their satisfaction with the company's approach to executive compensation.

We recommend that the Boards of companies voluntarily add to each annual meeting agenda an advisory resolution on the company's report on executive compensation. We also encourage companies to develop meaningful practices to increase engagement with all of their shareholders on this issue.

Where companies are required to hold or have voluntarily adopted an advisory vote on executive compensation policies, we will evaluate the companies' approach on a case-by-case basis to ensure that their compensation policies ensure fair compensation linked to performance.

#### **4.8 Compensation Consultants**

We will generally support shareholder proposals seeking disclosure regarding the company, Board, or Board committee's use of compensation consultants, such as company name, business relationship(s) and fees paid.

#### **4.9 Supplemental Executive Retirement Plans (SERPs)**

We will generally support shareholder proposals requesting to limit the executive benefits provided under the company's supplemental executive retirement plan (SERP) by limiting covered compensation to a senior executive's annual salary and excluding of all incentive or bonus pay from the plan's definition of covered compensation used to establish such benefits.

#### **4.10 Golden Parachutes**

Golden parachutes are severance compensation arrangements, to be paid to an executive whose employment is terminated in the event of a merger or acquisition that results in a change in control over the company. We will review severance compensation arrangements on a case-by-case basis. We will generally not support golden parachutes that provide for excessive severance compensation arrangements.

### **5. CAPITALISATION**

#### **5.1 Increase in Authorized Shares**

We will generally support proposals for the authorization of additional common shares provided the amount requested is necessary for sound business reasons. We will generally not support proposals that seek a 50% or greater increase in authorized common shares unless a viable corporate purpose is clearly provided.

## **5.2 Dual-Class Share Structures**

We believe that all shareholders should be treated upon the principle of one-share/one-vote. Therefore, we will generally not support the creation of a new class of common shares with superior voting rights, nor the extension of dual-class share structures.

## **5.3 Preferred Shares**

We will generally not support either the authorization of, or an increase in, a class of preferred shares with unspecified voting, conversion, dividend distribution and other rights, unless the amount of shares to be issued is limited and the issue is clearly in the best interests of the shareholders.

## **5.4 Pre-emptive rights, Private Placements and Share Buybacks**

We will generally support proposals for the issuance of shares with pre-emptive rights up to 50% of the issued capital, reasonable private placements and share buybacks.

## **6. MERGERS, CORPORATE RESTRUCTURINGS AND TAKEOVER PROTECTIONS**

### **6.1 Mergers and Corporate Restructuring**

We will evaluate mergers and corporate restructurings on a case-by-case basis based on such features as valuation assessments with emphasis on offer premium, strategic rationale, negotiating process, conflict of interest, changes in corporate governance and their impact on shareholder rights.

### **6.2 Takeover Protection - General**

We will evaluate takeover protection proposals, policies and plans on a case-by-case basis. We will generally support these takeover protection proposals, policies and plans if they ensure an equal treatment of shareholders in the event of a takeover offer and allow the company sufficient time to consider alternatives to an offer in order to enhance the shareholder value.

### **6.3 Reincorporation**

We will support reincorporation proposals when management and the Board of Directors can demonstrate sound financial or business reasons for the proposed change. However, we will generally not support reincorporation proposals that are made as part of an anti-takeover defence or solely to limit directors' liability.

## **7. SHAREHOLDERS' RIGHTS**

### **7.1 Confidential Voting by Shareholders**

We will support resolutions to introduce confidential voting.

### **7.2 Linked Proposals**

We will not support linked proposals the objective of which are to make one element of a proposal more acceptable.

### **7.3 Supermajority Approval of Business Transactions**

We will review supermajority proposals on a case-by-case basis but will generally not support proposals in which management seeks to increase the number of votes required on an issue above two-thirds of the outstanding shares.

### **7.4 Shareholders' Ability to Call Special Meeting**

We will not support proposals to restrict or prohibit shareholders' ability to call special meetings. Restricting or limiting such ability places shareholders in a disadvantageous position where they may lose an important right as the ability to remove directors or initiate a shareholder resolution without having to wait for the next scheduled meeting, if they are unable to act at a special meeting of their calling. The inability to call a special meeting and the resulting insulation of management could result in corporate performance and shareholder returns suffering. Conversely, we will support proposals that remove restrictions on the right of shareholders to act independently of management.

### **7.5 Shareholder Proposals**

We will evaluate shareholder proposals on a case-by-case basis. We will generally not support proposals that place constraints on the company, its Board, or management that do not serve the short or long term financial interests of the company or mitigate any of its financial risks.

We will generally support shareholders' proposals that seek to increase the Board of Directors level of accountability to shareholders.

## **8. RESPONSIBLE INVESTING**

Our approach to proxy voting seeks to be consistent with our Responsible Investment Policy. We will always take into consideration the principles set forth in our Responsible Investment Policy when addressing environmental social and governance ("ESG") issues that we may be requested to vote on from time to time. We believe that disclosure is the key that allows investors to better understand, evaluate and assess potential risks and return, including the potential impact of ESG factors on a company's performance. In all circumstances, we will support shareholder proposals that require full and timely disclosure of all policies, practices and matters that may materially affect shareholder value.