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BY EMAIL

August 27, 2012

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Alberta Securities Commission  
Saskatchewan Financial Services Commission  
Manitoba Securities Commission  
Ontario Securities Commission  
Autorité des marchés financiers  
New Brunswick Securities Commission  
Registrar of Securities, Prince Edward Island  
Nova Scotia Securities Commission  
Superintendent of Securities, Newfoundland and Labrador  
Superintendent of Securities, Northwest Territories  
Superintendent of Securities, Yukon  
Superintendent of Securities, Nunavut

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Dear Sir/Madam:

**RE: Consultation Paper 25-401: Potential Regulation of Proxy Advisory Firms**

This submission is made by the Public Sector Pension Investment Board ("PSP Investments") in reply to the consultation paper published on June 21, 2012 on the potential regulation of proxy advisory firms (the "Consultation Paper").

By way of background, PSP Investments is a Canadian Crown corporation established to invest the amounts transferred by the Government of Canada since April 1, 2000, for the pension plans of the Public Service, the Canadian Forces and the Royal Canadian Mounted Police, and since March 1, 2007, for the Reserve Force Pension Plan. To achieve its investment mandate, PSP Investments makes investments in public and private assets. As at March 31, 2012, PSP Investments' assets under management were worth over \$64.5 billion.

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## **General Comments**

We are pleased to have the opportunity to comment on the issues raised in the Consultation Paper. As a long-term institutional investor in the global equity markets, through proxy voting and active engagement with issuers, we promote better corporate governance and corporate responsibility with the objective of enhancing issuer performance and shareholder value.

Last year, PSP Investments voted globally at more than 2,900 shareholder meetings which represented over 30,000 resolutions. As part of the active management of our proxy voting activities, we review proxy circulars, reports from proxy advisory firms and other service providers and consult with our portfolio managers when voting the equities held in accounts managed internally as well as those in segregated accounts managed by external managers. PSP Investments uses the voting platform of a proxy advisory firm to ensure that all votes are submitted validly and on time, but PSP Investments retains at all times full voting authority.

We are not concerned about the role or current structure of proxy advisory firms. We feel that they provide a number of valuable services and generally promote good corporate governance practices. While their proxy advisor reports and voting recommendations may be a matter of interest to us, we evaluate matters on which we are entitled to vote carefully and cast our votes as we consider appropriate, in accordance with the Proxy Voting Guidelines adopted by our Board of Directors.

## **Specific Comments**

The following are our comments on the specific questions set out in the request for comments, which are reproduced below in italics.

### *1. Agreement with concerns identified in the Consultation Paper:*

#### *(i) potential conflicts of interest*

There is a perception from issuers that conflicts of interest exist with proxy advisor firms and that these conflicts of interest are not properly managed. Having had the opportunity to discuss this issue with proxy advisory firms, we do not have any reasons to believe that the ethical walls in place within proxy advisory firms or their internal processes are inefficient to manage properly conflicts of interest.

#### *(ii) perceived lack of transparency*

We do not think that transparency is a significant problem; proxy advisor reports disclose adequately the reasons for their vote recommendations.

#### *(iii) potential inaccuracies and limited engagement with issuers,*

As an institutional investor who actively manages its proxy voting, we expect to receive proxy advisor reports well in advance of the meeting to allow us enough time to review the issues at stake and speak to the issuers when necessary prior to casting our vote. Allowing an issuer to review a proxy advisor report is the best way to ensure that factual errors are caught and to ensure the issuer is made aware of any recommendations against management. However, we are cognizant of the fact that the short timelines between availability of proxy materials and voting deadlines provides only a short window of time to allow for a review by issuers.

*(iv) potentially inappropriate influence on corporate governance practices*

Proxy advisory firms develop their voting policies in conjunction with their clients and in some instances the issuers. The voting policies generally incorporate what is predominantly seen as best governance practices which is generally adapted to the standards of the local market. We feel that the influence of these voting policies has generally had a positive impact on corporate governance practices in Canada as issuers are paying attention to them. It is important to note that large institutional investors such as PSP Investments generally have their own proxy voting guidelines which may differ from those of the proxy advisory firm on many fronts.

*(v) the extent of reliance by institutional investors on the advice of such firms*

PSP Investments is employing the research services of more than one proxy advisory firm and does not rely exclusively on these proxy advisor reports when making its voting decisions. In addition to these reports, PSP Investments carefully reviews proxy circulars, consults its portfolio managers, conducts its own independent research prior to casting its vote. We believe that many institutional investors have a similar decision-making process.

2. *Are there other material concerns with proxy advisory firms that have not been identified?*

No

3. *Are there specific gaps in the current practices of proxy advisory firms which justify regulatory intervention? Is there a concern that future gaps could be created as a result of new entrants or changes in business or other practices?*

No

4. *Do you believe that the activities of proxy advisory firms should be regulated in some respects and, if so, why and how?*

Other than setting some guidelines for proxy advisory firms and basic rights for issuers as summarized under section 16 below, we do not see the need for extensive regulation. We encourage instead the regulators to look into a proxy voting reform to ensure the accountability, transparency and efficiency of the proxy voting system.

### ***Potential conflicts of interest***

5. *To what extent do you consider proxy advisory firms to:*

*(i) be subject to conflicts of interest in practice:*

For most proxy advisory firms, a perception of conflict of interest arises from time to time, but is isolated to specific proxies or situations.

*(ii) already have in place appropriate conflict mitigation measures:*

As discussed above, we believe that the ethical walls in place within proxy advisory firms and their internal processes are sufficient to manage any real or potential conflict of interest.

*(iii) be sufficiently transparent regarding the potential conflicts of interests they may face?*

Generally, proxy advisory firms have been thorough in disclosing where conflicts may occur in their proxy reports or by other means if it is not possible to do so in the body of the report.

6. *If you are of the view that there are conflicts of interest within proxy advisory firms that have not been appropriately mitigated, which of these are the most serious in terms of the potential (negative) impact on development of their voting recommendations and why?*

We are of the view that real or potential conflicts of interest are properly managed.

7. *Should we propose an amendment to NI 51-102 to require reporting issuers to disclose consulting services from proxy advisors in their proxy circular? Or would such disclosure undermine the existing controls and procedures (i.e., "ethical wall") in place which currently may prevent proxy advisory firm research staff who review an issuer's disclosure from being made aware of the identity of their firms consulting clients?*

No, we believe that it is better to maintain the existing controls and procedures (i.e. "ethical wall").

### ***Perceived lack of transparency***

8. *Could disclosure of underlying methodologies and analysis provide beneficial information to the market or would the commercial costs of doing so be too significant?*

No, we do not believe that the disclosure of the underlying methodologies and analysis will provide much benefit to the market.

### ***Issuer engagement***

9. *To what extent could there be an improvement in the dialogue with issuers during the vote recommendation process?*

We believe that issuers should have the opportunity to dialogue with the proxy advisory firms about a proposed resolution or a proxy advisor's recommendation. We also believe that issuers should be provided with a copy of the proxy advisory reports concerning an upcoming shareholder meeting.

10. *During proxy season, is it appropriate for a proxy advisory firm to engage with issuers in all circumstances or are there legitimate business and policy reasons why it should not be required to do so? Are there certain special types of situations where it is more important that issuers are able to engage with proxy advisory firms?*

If disclosure in the proxy circular is unclear or inadequate, proxy advisory firms, as should all shareholders, contact the issuer to obtain more information. If a proxy advisory firm recommends a vote against a management proposal or board nominee or in the event of a contested meeting, there should be an avenue available for the issuer to initiate dialogue with the proxy advisory firm. Our understanding is that this avenue already exists.

11. *If a proxy advisory firm, as a matter of policy, believes that there are certain circumstances where it is not appropriate for it to give issuers an opportunity to review its reports, would it be sufficient to only require in these circumstances that the underlying rationale for such policy be disclosed? Please explain. Or, alternatively should proxy advisory firms be required to provide issuers with an opportunity to review their reports in all circumstances?*

We believe that proxy advisory firms should provide issuers with the opportunity to review their reports in all circumstances and should provide an opportunity to dialogue with an issuer who has legitimate concerns.

12. *Should we prescribe the details of the processes that proxy advisory firms implement to engage with issuers? If so, what do you suggest the requirements should be?*

Other than ensuring the right to obtain a proxy advisor report and to provide an opportunity to dialogue with an issuer who has a legitimate concern, as noted question under 11 above, we do not believe that there should be any prescriptive steps.

### ***Potentially inappropriate influence on corporate governance practices***

13. *To what extent should there be a more fair and transparent dialogue between proxy advisors and market participants on the development of voting policies and*

*guidelines? Is it sufficient for proxy advisors to address governance matters by soliciting comments from their clients?*

We do not believe that proxy advisory firms have an inappropriate influence on corporate governance practices. We are of the view that their influence on the corporate governance debate has been positive as their voting recommendations have influenced issuers to adopt best governance practices. Feedback from clients, issuers and other market participants is, in our view, helpful when developing voting policies and guidelines. However, it is for the proxy advisory firm to develop its own voting policies and guidelines based on its own independent views.

***Proposed regulatory responses and framework(s)***

*14. Do you think a securities regulatory response is warranted in connection with each of the concerns identified above? Please explain why or why not.*

Other than setting some guidelines for proxy advisory firms and basic rights for issuers as noted above and summarized under section 16 below, we do not see the need for extensive regulation.

*15. Do you agree with the suggested securities regulatory responses to each of the concerns raised? If not, what alternatives would you suggest?*

See response under section 16 below.

*16. Do you agree or disagree with the requirements and disclosure framework set out in section 5.2.1 to address the concerns identified? If not, please indicate why. Would you prefer instead one of the other suggested securities regulatory frameworks identified above? If so, please indicate why. Do you agree or disagree with our analysis of these frameworks? Do you have suggestions for an alternative regulatory framework?*

We believe that proxy advisory firms already provide disclosure that the largely complies with the disclosure framework set out in section 5.2.1.

We believe that issuers should be provided with a copy of the proxy advisory reports concerning an upcoming shareholder meeting. Issuers should also have the opportunity to dialogue with the proxy advisory firms where a vote recommendation has been made against a management proposal, if there is a factual error in the report or if they have a legitimate concern.

While we do not have any reasons to believe that the ethical walls in place within proxy advisory firms or their internal processes are inefficient to manage properly conflicts of interest, if corporate services continue to be offered by proxy advisors, the proposal to separate proxy voting services from the advisory or consulting services, as contemplated in section 5.2.1 seems reasonable.

17. *Are you of the view that we should prescribe requirements in addition to or instead of those identified above for proxy advisory firms?*

No

***Additional questions for institutional investors:***

18. *To what extent and in what ways do you rely on the services provided by proxy advisory firms? Please be as specific as possible.*

We use the services of more than one proxy advisory firm for research purposes. We appreciate the detail of the reports and organization of data into a consistent form, making it possible to quickly identify areas where additional research or reference to the proxy circular is warranted. While their proxy advisor reports and voting recommendations may be a matter of interest to us, we evaluate matters on which we are entitled to vote carefully and cast our votes as we consider appropriate, in accordance with the Proxy Voting Guidelines adopted by our Board of Directors. As part of the active management of our proxy voting, we review proxy circulars, reports from proxy advisory firms and other service providers, consult our portfolio managers, conduct our own independent research and may engage with issuers before casting our vote.

We submit our votes using the voting platform of a proxy advisory firm. This service allows us to vote across all jurisdictions and to ensure that votes are submitted validly and on time.

19. *How do you view your duty to vote and how do the vote recommendations of proxy advisory firms play a part in your decision-making process?*

We believe that we have a duty to vote all proxies when feasible. Although, we review proxy advisor reports and voting recommendations, we make our own independent assessment of the issues and always vote in accordance with our Proxy Voting Guidelines which differ on certain matters from the voting policies of the proxy advisory firms.

20. *Do institutional investors have the ability to require changes to proxy advisory firms' practices without the need for regulatory intervention?*

Yes

21. *Assuming you share the concerns identified above, do lack of choice/competition or other market factors in the proxy advisory industry limit your ability to address these concerns directly such that regulatory intervention is warranted? Please explain.*

No.

22. *Given the above-noted concerns regarding the overall quality and lack of transparency underlying the vote recommendations of proxy advisory firms, what*

*measures do you take and, overall, how do you gain assurance that such recommendations are reliable for your voting purposes?*

PSP Investments is employing the research services of more than one proxy advisory firms and does not rely exclusively on these proxy advisor reports when making its voting decision. In addition to these reports, PSP Investments carefully reviews proxy circulars, consults its portfolio managers, conducts its own independent research and engages with issuers prior to casting its vote.

*23. Do you view the policy development process and resulting proxy voting guidelines of proxy advisory firms as appropriate and reflective of your governance preferences and views? Would input from issuers further benefit or potentially hinder such process?*

We agree that proxy advisory firms are influential and have positively contributed to the corporate governance debate. We believe that their policy development processes incorporate many factors and are subject to many influences whether from the client, issuer or regulator sides.

We appreciate this opportunity to comment on the Consultation Paper. Please do not hesitate to contact the undersigned if you wish to discuss any aspect of this letter in further detail.

Sincerely,



Stéphanie Lachance

Vice President, Responsible Investment and  
Corporate Secretary