Engaging for change
Active ownership report

Q1 2020

At NEI Investments, our ESG team actively engages companies across our funds to drive change on behalf of our investors. Through dialogue, we alert companies to the environmental, social and governance risks they are facing. We propose solutions to help them overcome tough challenges and improve their ESG performance, with the goal of protecting and growing value for shareholders. We also vote at Annual Shareholder Meetings on matters such as board appointments, good governance and shareholder proposals. This quarterly report shows the progress and outcomes of our engagement and policy activity.

Corporate engagement *by the numbers*

93 Shareholder meetings voted

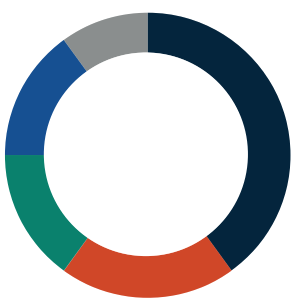
20 Focus List dialogues

6 Policy actions

Year to date

NEI engagement role

In Q1 we led 65% of our engagements, meaning that we either conducted the engagement ourselves, or led or co-led a collaboration with other investors. Leads are responsible for setting the agenda, and chairing and organizing the investor group's meetings with a company.



- 38% Solo
- 24% Collaborative Light Participant
- 14% Collaborative Co-Lead
- 14% Collaborative Active Participant
- 10% Collaborative Lead

Vote instruction

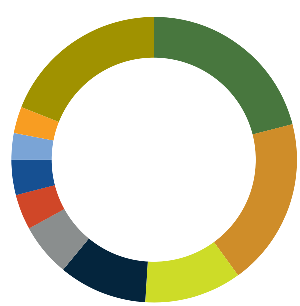
In Q1 we voted against company management on 27% of agenda items at Annual Shareholder Meetings. Voting against management is one indicator to determine whether proxy votes are actively managed by a fund company, rather than set to automatically vote in favour of management.

- 71% With management
- 27% Against management

Engagement by sector

- 38% Energy
- 14% Financials
- 14% Industrials
- 10% Information Technology
- 10% Health Care
- 9% Consumer Discretionary
- 5% Materials

Votes by market



- 21% U.S.
- 19% South Korea
- 11% Canada
- 10% Japan
- 6% Brazil
- 4% Sweden
- 4% Switzerland
- 3% Denmark
- 3% India
- 19% Other

To learn more about how we voted at companies in a particular fund and to review our voting guidelines, visit our proxy voting section at neiinvestments.com.

COVID-19 crisis presents opportunity to create lasting positive change

By David Rutherford, VP of ESG Services

The first quarter of 2020 had just one storyline: COVID-19.

It's clear that whatever assumptions we made about life, business, the economy, companies, the environment – you name it – can and should be tossed aside. They no longer apply. In the space of a few months, a single virus has changed everything, and we can't go back to the way things were. We can only move forward.

We get this implicitly. At NEI we are wired to look to the future, and to help create what we believe is a better future. That's why it's natural for us to look forward instead of back. It's built into our culture.

And it is our culture that colours the way we look at the COVID-19 crisis. We, of course, see the devastation – in personal terms, to our health care system, and to our economy – that the virus is causing. But we are also looking beyond the crisis to consider the actions we can take to turn this crisis into an opportunity for positive change, including:

- Using promised financial support to invest in an energy infrastructure that will accelerate the growth of sustainable solutions
- Reaching out to applaud those companies for their actions during the crisis, and helping them embed the forward-looking business practices that have become a hallmark of the crisis response
- Revisiting issues like share buybacks, executive compensation and responsible taxation to ensure companies exit the crisis with more sustainable structures in place

The COVID-19 crisis has already accelerated the move toward stakeholder capitalism – an approach to company operations that seeks to add value for all stakeholders, not just shareholders – something we were seeing only glimpses of before. Prior to the virus, we heard a lot of progressive talk from business leaders like Larry Fink of BlackRock and the CEOs of the Business Roundtable, but that was all it was – talk. Now, in the midst of crisis, many corporate leaders are putting those words and the principles of stakeholder capitalism into action.

This is an approach to business we've long advocated for, and built into our company engagements. And as we come out of crisis and look to re-build the economy and investor confidence, we'll be staying on top of these developments to determine if the changes we're seeing now are, in fact, a new way of doing business inspired by the crisis, or merely a short-term response to it.

That difference is important to us. As shareholders ourselves, it is our job to help companies understand that providing value to all stakeholders will make them more sustainable businesses and better long-term investments. And we'll be using our decades of engagement experience to nurture the "green shoots" of stakeholder capitalism we're seeing now and encourage all companies to make this their core operating philosophy.

We're not claiming victory on this front. Not yet. We know the economic and social fallout of this pandemic will inevitably lead to some very tough choices for companies, and for Canadians. We fully recognize what we're all up against. Solving the short-term crisis is paramount, and we're respecting that need within the companies we were slated to engage with in Q1. We've pulled back to allow them to focus on immediate, crisis-driven needs.

Instead we're using this as an opportunity to shine a light on the good things that are happening and the great things that companies are doing for their stakeholders. We'll showcase this work in our future engagements, turning that inspiration into aspiration and in the process use this crisis as an unparalleled opportunity to create lasting positive change.

Responsible tax: Can companies ask for more when they pay less?

By Hasina Razafimahefa, Senior ESG Analyst

With the devastating impact of COVID-19 on the economy, government stimulus to support companies in weathering this crisis is vital. Stimulus, however, is a two-way street. Massive corporate bailouts on the scale of those promised in the wake of COVID-19 drive home just how critical it is for governments to nurture a healthy tax system. And that includes ensuring companies pay their fair share of taxes.

We have strived to consistently address this issue over the past years. Most recently, as part of the collaborative engagement the PRI coordinated among investors representing US$2.9 trillion in assets from 2017 to 2019, we took a leading role to raise concerns about aggressive corporate tax practices, urge companies to adopt responsible tax practices, and ask for improved disclosures on tax policy, governance and financial reporting. As highlighted in the PRI report released in March 2020, only 27 of the 41 targeted multinational companies in the healthcare and technology sectors made a commitment to avoid aggressive tax planning. Only five companies explained their approach to tax havens. And not a single company produced a country-by-country tax report.[1]

The COVID-19 crisis has laid bare significant issues that we must address if we are going to move forward in building a healthier, sustainable economy. Addressing the critical need for structural changes in tax transparency and corporate tax practices is among them. Clearly there is much more work to do on this front.

[1] Advancing tax transparency: outcomes from the PRI collaborative engagement 2017-2019, Principles for Responsible Investment (PRI)

Net zero or bust

By Jamie Bonham, Director of Corporate Engagement

Before COVID-19 threw the world into a tailspin, there was some much needed momentum building on the other systemic crisis – climate change. Specifically, the end of 2019 and early 2020 saw several major emitters in Canada – Canadian Natural Resources (CNRL), Cenovus Energy and Teck Resources – issue public commitments to reach net-zero emissions. These commitments align with Canada's commitment under the Paris Agreement to be net-zero by 2050 and follow similar commitments made by several of the European-based O&G majors.

Recognizing that any commitment that reaches out to 2050 is by nature aspirational, the importance of a shared ambition shouldn't be downplayed. The net-zero commitment is a key aspect of our engagement program and we hope to see it become the standard by which climate-related targets are judged.

But what's in a target?

Each of the companies took a different tack in making their commitment, and we will be taking a deeper dive into the commitments in our dialogues. CNRL set some interim intensity-based targets in response to our ask for a pathway to net-zero, but hasn't committed to the 2050 timeline nor addressed the issue of absolute emissions. Cenovus also announced intensity-based targets (30% by 2030) but attached a goal of keeping absolute emissions flat over that same period. While that commitment may not sound like much, it is the first absolute-based emissions reduction target in the North American oil patch. And Teck stated it is in the process of setting 2025 and 2030 interim goals, which could possibly address absolute emissions.

All have indicated they will be working on providing greater clarity for investors on the potential technological/operational pathways to net-zero. (Teck announced around the same time a commitment to purchase enough renewable energy to power half its energy needs at its Quebrada Blanca Phase 2 project in Chile, while also purchasing outright the SunMine solar energy facility operating on its remediated Sullivan mine site, an indication that renewables will play a role in their strategy.)

Outstanding are some big questions about what role, if any, carbon offsets should play in a net-zero target and whether the commitment should cover Scope 3 emissions (i.e., the emissions associated with the end use of their products – which in the case of oil is roughly 80% of the emission profile). These will be challenging topics with no easy answers, and the dramatic cuts in capital spending being announced in response to the current crisis will certainly delay some of the planned developments. However, while the COVID-19 crisis will surely pass, the climate crisis is just ramping up. The imperative to be a part of a net-zero future is only going to grow and will remain a central ask in our dialogues.

Enbridge steps up

In February we attended a half-day workshop held by Enbridge to discuss what a credible commitment to net-zero could look like for a company in the mid-stream sector. Other attendees included O&G companies and service providers, environmental NGOs, sustainability consultants, and government representatives. The workshop was a substantive dive into how the company could achieve a net-zero vision and what constitutes a credible path.

This discussion is an extension of the dialogue we have held with the company asking them to set ambitious climate-related targets, and we were pleased to see the company taking this innovative approach. We used the workshop to encourage the company to ensure the targets it sets are ambitious enough to drive the kind of transformative change required to be resilient in a low-carbon future.

From $4 billion to $750 billion on sustainable finance commitments: What do we expect from banks?

By Hasina Razafimahefa, Senior ESG Analyst

In March, we met with Goldman Sachs in collaboration with other investor members of the Interfaith Center on Corporate Responsibility (ICCR) to discuss, among other environmental and social issues, the firm's recent sustainable finance commitment: US$750 billion by 2030 to promote inclusive growth and climate transition. Goldman believes these two growth themes will play an increasingly significant role in the economy and for its clients. Its target, which includes direct financing, investing and advisory services, is significantly higher than that of any other bank.

We are pleased to see more banks announce sustainable financing targets every year, although to date those setting such targets represent only half of the world's 50 largest private sector banks. In Canada, TD was the first major Canadian bank to set a low-carbon financing target in 2017, followed by the rest of the "Big 5" (RBC, BMO, CIBC and Scotiabank) in 2019. Over the past few years, we have been engaging these banks on the role they play in advancing the transition to a low-carbon economy.

Setting an ambitious target for low-carbon financing is a key step to drive meaningful change. Furthermore, rather than merely divesting from oil and gas companies, we expect banks to use their financial leverage to help transform these companies, by helping drive clean technology innovation in their operations and explore further climate-related opportunities in other sectors.

But a sustainable finance commitment alone is not enough to determine the impact that a bank really has. Existing commitments vary widely in size, scope and structure. Some banks like TD and Goldman Sachs are specific on what sectors or themes they are targeting whereas others are not. Also, only half of North American banks with existing targets disclose an accounting methodology to track their different financing activities toward their commitment.

Although there is still no widely accepted accounting methodology for sustainable finance, we expect more from banks: that they be more transparent on how they implement their targets and track their sustainability impact. This is something we will continue to review and engage with banks on as they start or progress in their low-carbon financing journey.

Should share buybacks be 'quarantined'?

By Lucia Lopez, ESG Analyst

As balance sheets become increasingly constrained amid the COVID-19 pandemic, many companies are looking to government support to stay afloat. But it's important to understand exactly how that money will be used.

For example, recent research has shown that over the past decade U.S. airlines have spent one third more than the amount they are currently seeking in financial support from the U.S. government as a result of the pandemic, on share buybacks. (A share buyback is a transaction whereby a company buys back its own shares from the marketplace, often because company management believes its shares are undervalued.) Since 2010, U.S. airlines have purchased US$79 billion in buybacks. As of this writing, they are seeking US$54 billion in support from the federal government.[1]

However, airlines are not alone in this practice. Buybacks have increased significantly across all industries in the past 10 years.[2] While buybacks per se are not an inappropriate practice, concerns arise when investments in other business areas are, or could be sacrificed as a result of committing corporate cash to buybacks.

More concerning is the close link between buybacks and executive compensation. By removing shares from the market, buybacks can boost the earnings per share (EPS) of a company's stock, often one of the metrics that determines the level of executive compensation. A good signal is that the U.S. Coronavirus Aid, Relief, and Economic Security Act (CARES Act) attaches specific conditions around capital distribution and executive compensation to those companies borrowing under its provisions.[3]

This is an especially important consideration in light of COVID-19. Crises are often the catalysts for change; they can accelerate processes as they necessarily provoke reflection on the status quo. As such, conversations around rethinking executive compensation are starting to emerge. While we acknowledge that companies are dealing with pressing challenges as a result of the pandemic, we also recognize the current circumstances are fertile land to consider structural reforms.

At NEI, governance is an overarching focus of our corporate engagement work. We believe good governance is the pillar upon which long-term corporate success is built. Moreover, good governance is directly linked to the executive compensation structure and capital allocation of companies. The work of boards is crucial in determining the appropriate balance between short- and long-term incentives for executive compensation. What is evident is that current incentive structures have not made companies resilient.

The resiliency risk embedded in current compensation mechanisms merits thinking about which metrics are best suited to measure the performance – and determine the compensation – of senior executives. A good starting point would be to reflect the provisions of the CARES Act, and "quarantine" all share buybacks; or, at the very least, review the weighting of buyback-influenced EPS as a driver of executive compensation. A longer-term objective could be subjecting buybacks to a shareholder to vote, implementing a similar approach to the "say-on-pay" vote structure that already exists.

According to our data, in the 2019 proxy season in North America, we saw two proposals regarding disclosing executive compensation metrics for share buybacks put forward by shareholders. Voting on capital redistribution is not unusual in European and Asian markets, where we saw nearly 300 proposals related to dividends during the same period.

How companies compensate their executives remains a core ESG issue. In addition to being proponents of directly linking compensation to ESG outcomes, we also believe it is an opportune time to ponder deeper questions regarding the future structure of executive compensation and would recommend the role of share buybacks be a part of that discussion.

[1] "Impact of COVID-19 on INCENTIVE COMPENSATION." Institutional Shareholder Services, April 7, 2020. https://www.isscorporatesolutions.com/file/documents/ics-the-impact-of-covid-19-on-incentive-plans.pdf.

[2] Ibid.

[3] BakerMcKenzie. "CARES Act 2020: Federal Reserve Measures in Response to COVID-19: Insight: Baker McKenzie," March 31, 2020. https://www.bakermckenzie.com/en/insight/publications/2020/03/cares-act-federal-measures-covid19.

Guiding corporate sustainability strategies

This quarter we responded to several companies who proactively reached out to us for feedback on their sustainability strategies.

3M asked us (before the virus outbreak) to participate in their materiality assessment where, among other priorities, we highlighted our support for their commitment to have 100% of their new products created with a demonstrable sustainability goal in mind, and emphasized the importance of working to address their plastic footprint and looking for opportunities to lead in the move to a circular economy.

AltaGas reached out to get our perspective on their most material issues, and we highlighted the company's opportunities in the energy transition, and specifically highlighted the role of reducing methane emissions and the opportunity to partner with Indigenous communities in low-carbon technologies.

Teck Resources approached us to get our feedback on their new sustainability strategy, ranging from their tailings management plan to their climate change goals and targets. We noted our appreciation for the company's goal of achieving carbon neutrality by 2050 and encouraged the company to provide clear interim targets to guide its progress. We also encouraged the company to take a deeper look at the role it could play in a circular economy.

Corporate *dialogues*

Holdings can change at any time without notice.

Company	Sector	Topic	NEI funds
3M	Industrials	Plastic solutions	NEI Tactical Yield Fund; NEI U.S. Dividend Fund
Alphabet	Information Technology	Human rights due diligence	NEI Global Equity Fund; NEI Global Equity Pool; NEI Global Equity RS Fund; NEI U.S. Equity Fund; NEI U.S. Equity RS Fund
AltaGas	Energy	Advancing ESG management and disclosure; Implementing TCFD recommendations on climate disclosure	NEI Balanced RS Fund; NEI Canadian Equity RS Fund; NEI Canadian Small Cap Equity RS Fund
Bank of Montreal	Financials	Advancing the Canadian energy transition; responsible lending	NEI Canadian Dividend Fund; NEI Jantzi Social Index Fund
Bristol-Myers Squibb	Health Care	Access to Medicine Index	NEI Global Equity Pool; NEI Tactical Yield Fund; NEI U.S. Dividend Fund; NEI U.S. Equity RS Fund
Canadian Natural Resources	Energy	Human rights due diligence	NEI Balanced RS Fund; NEI Canadian Dividend Fund; NEI Canadian Equity Pool; NEI Canadian Equity RS Fund
Canon	Information Technology	Human rights due diligence	NEI Global Dividend RS Fund
Cenovus Energy	Energy	Advancing the Canadian energy transition	NEI Balanced RS Fund; NEI Canadian Dividend Fund; NEI Canadian Equity RS Fund; NEI Jantzi Social Index Fund
Chevron	Energy	Human rights due diligence	Sold
ConocoPhillips	Energy	Advancing the U.S. energy transition; respecting Indigenous rights	NEI Global Equity Fund; NEI U.S. Equity Fund
Enbridge	Energy	Advancing the Canadian energy transition	NEI Balanced RS Fund; NEI Canadian Dividend Fund; NEI Canadian Equity Pool; NEI Canadian Equity RS Fund
Ford	Consumer Discretionary	Investor Decarbonisation initiative; Climate Action 100+	NEI Global Equity RS Fund
General Electric	Industrials	Investor Decarbonisation Initiative	NEI Canadian Equity Fund
Goldman Sachs	Financials	Advancing ESG management and disclosure	NEI Global Value Fund; NEI U.S. Equity Fund
Kuehne & Nagel International	Industrials	Investor Decarbonisation Initiative	NEI International Equity Fund
Marathon Petroleum	Energy	Climate Action 100+	NEI Tactical Yield Fund; NEI U.S. Dividend Fund
Marriott International	Consumer Discretionary	Investor Decarbonisation Initiative	NEI U.S. Equity Fund
Pfizer	Health Care	Investors for Opioid Accountability	NEI Tactical Yield Fund; NEI U.S. Dividend Fund
Precision Drilling	Energy	Advancing ESG management and disclosure	NEI Canadian Equity Fund; NEI Growth & Income Fund
Royal Bank of Canada	Financials	Responsible lending; advancing the Canadian energy transition	NEI Balanced RS Fund; NEI Canadian Dividend Fund; NEI Canadian Equity Fund; NEI Canadian Equity Pool; NEI Canadian Equity RS Fund; NEI Global Dividend RS Fund; NEI Global Equity Pool; NEI International Equity Fund; NEI Jantzi Social Index Fund
Teck Resources	Materials	Advancing the Canadian energy transition; advancing ESG management and disclosure	NEI Balanced RS Fund; NEI Canadian Equity RS Fund; NEI Jantzi Social Index Fund

Policy *actions*

Policy activity	Impact sector	Impact market	SDG theme
We participated in the PRI's consultation on its proposed Active Ownership 2.0 framework, an aspirational standard for improved stewardship. The PRI is looking to develop a standard that enhances the focus on engagement outcomes.	Investors	Global	SDG 16 - Peace, justice and strong institutions
We participated in the PRI's consultation on proposed changes to the PRI Reporting Framework. The PRI is looking to raise the bar for what constitutes RI leadership while also looking to make the framework less onerous and more useful to signatories.	Investors	Global	SDG 16 - Peace, justice and strong institutions
We joined a sign-on letter organized by the Interfaith Center on Corporate Responsibility, outlining our concerns about the rollback of environmental protection legislation in the U.S.	All	U.S.	SDG 13 – Climate action
We joined a sign-on letter organized by the PRI in response to proposals from the U.S. Securities and Exchange Commission that would result in restricting shareholder rights to file resolutions, among other things.	All	U.S.	SDG 16 - Peace, justice and strong institutions
We were invited to provide feedback to Global Affairs Canada on its Responsible Business Conduct strategy, indicating our support for enhancing the strategy's alignment with the UN Guiding Principles on Business and Human Rights and on extending the government's focus to the information and communication technology sector.	All	Canada	SDG 16 - Peace, justice and strong institutions
We joined a statement organized by the Interfaith Center on Corporate Responsibility regarding investor expectations of companies as they respond to the COVID-19 crisis, highlighting the need to put stakeholders at the centre of their strategic response.	All	Global	SDG 16 - Peace, justice and strong institutions

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