PHILLIPS, HAGER & NORTH
Investment Management®

PH&N Community Values Funds: Investment Principles

RBC Global Asset Management

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Introduction

The PH&N Community Values Funds are a family of four funds that invest primarily in the securities of companies that conduct themselves in a socially responsible manner.

The Community Values Investment Principles set out the screening criteria by which the social and environmental performance of companies is assessed. Companies who score poorly against these criteria are placed on the Prohibited Securities List, which is a list of companies whose securities cannot be held in the PH&N Community Values Funds. Phillips, Hager & North Investment Management (PH&N IM), in consultation with Sustainalytics, developed the Community Values Investment Principles. Sustainalytics is responsible for assessing the performance of companies against the Community Values Investment Principles. Investment decisions are solely the responsibility of PH&N IM.

The Community Values Investment Principles reflect what we believe are the most important environmental, social and governance (ESG) issues of concern to Canadians. We may modify or add to these Investment Principles at our discretion to reflect the evolution of community views on social, environmental and other issues.

Analytical Framework

The Community Values Investment Principles outlined in the next section are divided into two basic types: *exclusionary screening criteria and qualitative screening criteria*.

Exclusionary Screening Criteria

Exclusionary screening criteria are used to screen out companies that manufacture products and/or provide services that social investors may wish to avoid. The screening criteria proposed in the next section include involvement in the areas of alcohol, gambling, military weapons, pornography, and tobacco. Most are based on a threshold of involvement that is defined in terms of percentage of annual revenues. Any company that meets any of the exclusionary screening criteria will be placed on the Prohibited Securities List and thus will not be eligible for inclusion in the PH&N Community Values Funds, regardless of any positive aspects of the company's social and environmental performance.

Qualitative Screening Criteria

Qualitative screening criteria are applicable to areas such as community, employee relations and environment, in which it is possible for a company to perform both positively and negatively. It is therefore possible to implement *positive screening criteria* – that is, screening criteria designed to select companies with desirable attributes – as well as *negative screening criteria* – that is, criteria designed to screen out companies with undesirable attributes. The inclusion of positive screening criteria reflects one of the goals of most social investors, which is to focus not only on screening out companies with poor records, but also on encouraging positive social performance by "screening in."

The application of qualitative criteria involves evaluating each company's overall performance, both positive and negative, in each issue area. In the area of employee relations, for example, exceptionally strong employee benefits and programs may offset a less than perfect union relations record. The application of qualitative screening criteria may also involve balancing strengths and concerns across issue areas. For example, strong performance in the area of employee relations may be sufficient to offset a weak environmental record.

On the basis of such evaluation, the qualitative screening criteria listed in the next section are used to screen in companies that, on balance, have positive social and environmental records and screen out companies that, on balance, have poor records.

The Best-of-Sector Methodology

Criteria in two areas – specifically, occupational health and safety and environmental performance – are based on a *best-of-sector* approach, in which each company's record is evaluated in relation to that of its industry counterparts. The standard for performance is the best practices in its industry.

As part of its performance assessment, Sustainalytics uses the best-of-sector approach to evaluate safety and environmental records because, in both of these areas, companies in certain sectors face challenges that are inherent to the nature of the operations of their sector. For example, a company within the forestry sector is not expected to eliminate all negative environmental impact, because it is measured against the standard of best practices in its sector.

The best-of-sector approach is consistent with one of the general goals of social investment, which is to effect positive social change. The best-of-sector approach facilitates engagement with companies in sectors that have a high level of exposure to certain safety or environmental issues. It sends the message to such companies that they are not expected to be "perfect" (i.e., to eliminate all safety concerns or environmental impact). Instead they are expected to adhere to the best practices of their industry, and if they do so they will be eligible for investment. Thus, the best-of-sector approach can provide an incentive for companies in industries facing safety and environmental challenges to improve their performance.

Community Values Investment Principles

The Community Values Investment Principles are organized into two major parts.

Exclusionary screening criteria:

- Alcohol
- Gaming
- Military weapons
- Pornographic materials
- Tobacco

Qualitative screening criteria:

- Community
- Corporate governance
- Employee relations
- Environment
- Human rights
- Product safety

Exclusionary Screening Criteria

PH&N Community Values Funds will avoid investing in the securities of companies meeting any of the criteria listed below.

(i) Alcohol

- The company is directly involved in the production of alcoholic beverages and 5% or more of its revenue comes from this activity.
- The company derives 10% or more of its revenue from activities related to the production of alcoholic beverages, which may include the indirect involvement through a subsidiary.
- The company derives 10% or more of its revenue from the sale of alcoholic beverages.

(ii) Gaming

- The company is directly involved in the gaming or lottery industries and 5% or more of its revenue comes from this activity.
- The company derives 10% or more of its revenue from the production of goods and services related to gaming or lottery industries, which may include the indirect involvement through a subsidiary.

(iii) Military Weapons

- The company develops and/or manufactures weapons and 5% or more of its revenue comes from this activity.
- The company manufactures weapons-delivery systems (such as jet fighters, battleships, military submarines, tanks, and armoured personnel carriers) and 5% or more of its revenue comes from these activities.
- The company derives 5% or more of its revenue from the design and/or manufacture of specialized components of weapons.
- The company derives 10% or more of its revenue from the design and/or manufacture of non-specialized components of weapons or of components/parts for weapons delivery systems, which may include the indirect involvement through a subsidiary.
- The company derives 10% or more of its revenue from the provision of support services for weapons delivery systems, such as the repair and overhaul jet fighters, military flight training services, etc., which may include the indirect involvement through a subsidiary.

(iv) Pornographic Materials

- The company is directly involved in the production of pornographic materials and 5% or more of its revenue comes from this activity.
- The company derives 10% or more of its revenue from the production of goods and services related to pornography, which may include the indirect involvement through a subsidiary.
- The company derives 10% or more of its revenues from the sale of pornographic materials.

(v) Tobacco Products

- The company manufactures tobacco products and 5% or more of its revenue comes from this activity.
- The company derives 10% or more of its revenue from the production of tobacco-related products, which include the indirect involvement through a subsidiary.
- The company derives 10% or more of its revenue from the sale of tobacco products.

Qualitative Screening Criteria

Evaluating a company's performance in relation to qualitative criteria involves assessing a company's overall performance, both positive and negative, in each issue area. It may also involve balancing strengths and concerns across issue areas. PH&N Community Values Funds will seek to invest in companies that, on balance, have positive records according to the following criteria.

(i) Community

The word "community" refers primarily to the residents of local communities in which a company operates. In the case of many resource companies in Canada, this often means local First Nations communities upon whose traditional land a company is operating. The word "community" may also refer to the larger areas, such as a province or nation, to the extent that society in such larger areas is affected by a company's operations.

Positive screening criteria

- The company contributes directly to the development of communities in which they operate through donations or community investment programs.

Negative screening criteria

- The company has ignored or failed to take into account the needs and interests of communities affected negatively by its operations or planned operations. Evidence of such failure may be found in a lack of engagement in public consultation, especially in the face of community opposition, or in fines, civil penalties, or civil suits related to a company's negative impact on communities.
- The company has ignored or failed to take into account the needs, interests, and rights of aboriginal communities affected by its operations or planned operations.

(ii) Corporate Governance

Strong corporate governance practices enhance investor confidence in a company. They also help to prevent abusive corporate practices. PH&N Community Values Funds will primarily support the development of good corporate governance practices through the voting of proxies in support of effective corporate governance practices. The Funds may nonetheless screen out companies with exceptionally poor governance practices.

The assessment of corporate governance practices will give consideration to numerous elements including the following:

- The development and implementation of corporate governance principles.
- A strong code of business conduct.
- The level of independence on the Board.
- The level of independence on key Board committees.
- Whether or not the roles of chairman and CEO are separated.
- The presence of a confidential proxy voting procedure.
- The company's share structure.
- The level of compensation of the highest-paid executives.
- The presence of excessive termination agreements.
- Potential dilution that may result from the company's stock option plan.
- Any involvement in controversies over corporate governance practices.

(iii) Employee Relations

Positive screening criteria

- The company offers a comprehensive benefits package to its employees. In addition to basic benefits, such benefits may include programs to encourage employee ownership (through stock option or share purchase plans), profit sharing plans, wellness programs and policies that address the importance of a work/life balance.
- The company has implemented policies and management systems to ensure the health and safety of its employees.

Negative screening criteria

- The company provides inadequate benefits to its employees.
- The company has a health and safety record that is poor relative to its industry counterparts.
- The company has poor relations with its unionized workers, including a recent history of contracting out unionized jobs, first contract arbitration hearings, strike activity, or unfair labour practices. Or, the company has engaged in anti-union activity in opposition to attempts on the part of some workers to become unionized.
- The company has faced major controversies or legal action related to discrimination in the workplace or employment equity issues.

(iv) Environment

PH&N Community Values Funds will avoid investing in companies whose environmental performance is poor relative to their industry counterparts. In most industries, a company's environmental performance is considered "poor" if it ranks in the bottom third of its industry.

In assessing each company's environmental performance, consideration will be given to the following elements:

- Environmental management and reporting systems.
- The company's record of compliance with applicable environmental laws, regulations, and operating permits.
- Methods of use/extraction of natural resources (this includes consideration of the use of recycled materials in production processes, the use of alternative energy sources, or resource extraction methods that minimize environmental impact).
- Level of emissions of hazardous or toxic substances or substances that contribute significantly to ozone depletion or the formation of acid rain.
- Impact on natural ecosystems, including the health and viability of wildlife populations (this includes consideration of development projects or other planned operations that are likely to have such an impact).
- Measures to reduce the environmental impact of operations (this includes consideration of reductions in the use and/or release of toxins, hazardous substances, and other pollutants).
- The impact of the company's product (this includes consideration of the provision remediation or other environmental services, or products with environmental benefits, as well as the manufacture of products, such as pesticides or other harmful chemicals, that have a negative impact on the environment).
- Disclosure of greenhouse gas (GHG) emissions.
- Efforts to reduce GHG emissions and/or mitigate GHG emissions.
- Disclosure of business risks associated with GHG emission constraints that have been or may be imposed.

(v) Human Rights

Positive screening criteria

- The company has implemented a code of conduct that addresses human rights issues relevant to its operations in countries with poor human rights records.
- The company has implemented a code of conduct that addresses human and labour rights issues related to its supplier relationships.
- The company has implemented mechanisms to ensure compliance with its human rights code(s) of conduct.
- The company has implemented a code of conduct for operations in a conflict zone.
- The company has management structures and systems in place to ensure compliance with the code of conduct.

Negative screening criteria

- There is substantial evidence that the company has been complicit in the violation of human rights.
- The company has operations in Burma that create significant exposure to human rights issues there. Such exposure may result from involvement in sectors including, but not limited to, resource extraction and infrastructure development.
- The company is involved directly or through its major suppliers in the use of child, forced, or "sweatshop" labour.
- There is substantial evidence that the company has been complicit with military or paramilitary organisations participating in the conflict. This would include the provision of funding, logistics, or equipment either directly or indirectly to the parties.
- The company operates in a conflict zone and there is substantial evidence that its operations there are exacerbating the conflict.

(vi) Product and Business Practices

Positive screening criteria

- The company has a written/formal code of ethics or business conduct, as well as mechanisms to ensure compliance with the code, such as training for all employees, an annual review and sign-off on the code by all employees, etc.
- The company has a formal policy on bribery and corruption.

Negative screening criteria

- The company has regularly engaged in fraudulent, deceptive, or highly controversial marketing or advertising practices.
- The company has been convicted or paid recent fines or civil penalties related to price fixing, antitrust violations, or other illegal business activities.
- There is a clear pattern of negligence concerning the safety of one or more of the company's products. Evidence of this would include multiple lawsuits and regulatory actions that allege the company's products have caused life-threatening injuries, illness or death while being used responsibly and for their intended use.
- There is substantial evidence of the company's involvement in bribery or corruption.

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