

Deputy Prime Minister
and Minister of Finance



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Ottawa, Canada K1A 0A2

2024-04-11

Mr. Ken Hardie, M.P.

Chair

Special Committee on the Canada-People's Republic of China Relationship

House of Commons

Ottawa, Ontario

K1A 0A6

Dear Mr. Hardie:

Pursuant to House of Commons Standing Order 109, I am pleased to submit on behalf of the Government of Canada the response to the fifth report by Special Committee on the Canada-People's Republic of China Relationship (the Committee), entitled: *The Exposure of Canadian Investment Funds to Human Rights Violations in the People's Republic of China* (the Report).

The Government expresses its appreciation to the members of the Committee for their dedication and valuable work in examining the exposure of Canadian investment funds to human rights violations in the People's Republic of China (PRC).

The Government also extends its gratitude to the many witnesses, including advocacy groups, experts, pension funds, government officials, and others who appeared before the Committee or provided written briefs. The Committee's analysis, supported by the witnesses' insights, provides an informed perspective on this issue.

The Government of Canada remains committed to taking action to promote human rights globally and ensuring Canada is not complicit in human right violations. This commitment is demonstrated through Canada's support of the United Nation's (UN) 2022 assessment of human rights in Xinjiang, and the recent enactment of the *Fighting Against Forced Labour and Child Labour in Supply Chains Act*, as well as the various government initiatives that have been put in place to tackle exploitation in Canadian supply chains.

The Government welcomes the Committee's Report and supports in principle all the Committee's recommendations. The seven recommendations contain important insights that will be instrumental in considering future government policy. To that end, please

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find below the Government's Response to the Committee's recommendations. A detailed response to each recommendation is included in an Annex.

The Government is committed to continue its ongoing work to improve the transparency and oversight of pension fund investment decisions. Canada is home to many of the world's largest and most successful pension funds. They have achieved this reputation by making sound investment decisions and carefully managing risks. Maintaining this reputation and protecting Canada's world-class retirement income system requires constant vigilance, both by pension funds and by the federal and provincial governments.

Given geopolitical developments and shocks to global supply chains in recent years, pension funds are re-evaluating their investments around the world. While the potential returns of emerging markets once overshadowed the many risks, those risks are now top of mind for Canadian pension fund managers.

Investments in companies and regions that pose legal, geopolitical, national security risks, or do not take human rights and corruption seriously present a long-term risk to pension plan beneficiaries. Pension fund managers have a duty to account for these risks in their investment decisions. It is critical for the retirement security of Canadians and the future prosperity of Canada. It is also consistent with Canadian values.

The first three of the Committee's recommendations relate to developing lists of companies deemed unsuitable for investment or entities that Canadian public pension funds would be prohibited from investing in due to risk to national security, corruption or gross human rights violations.

The Government agrees with the importance of increased scrutiny of pension fund investments and of ensuring that public pension funds do not invest in companies or regions that present national security, corruption, or gross human rights violation risks. Certain companies and regions pose such high risks that they do not present suitable investments for pension plans. The Government's approach to the oversight of pension funds and to addressing these risks through a variety of tools is aligned with and demonstrates its commitment to this objective.

The strong governance and robust federal and provincial oversight frameworks for pension plans are key contributors to the success of Canada's world-class retirement income system. Large public pension funds apply leading investment practices by taking environmental, social, and governance (ESG) risks into account and incorporating aspects of human rights into their due diligence procedures. Additionally, the Government uses the tools at its disposal to promote human rights, including the *Special Economic Measures Act* (SEMA), which lists and prohibits transactions with entities that have been sanctioned for gross and systemic human rights violations including the use of forced

labour in the Xinjiang Uyghur Autonomous Region (XUAR), and the recently enacted *Fighting Against Forced Labour and Child Labour in Supply Chains Act* (the Supply Chains Act).

The Government has committed to deepen transparency on how federally regulated plans consider environmental, social, and governance (ESG) factors in their investment decisions. The Government has also committed to improve disclosures of federally regulated pension plans related to where they invest around the world and their crypto-asset holdings, and to engage with provinces and territories to discuss similar disclosures by Canada's largest pension plans.

The fourth recommendation relates to the Government's commitment in Budget 2023 to, by 2024, propose legislative changes and enhanced enforcement to eliminate forced labour from Canadian supply chains and to reinforce the prohibition on the import of goods produced by forced labour. Canada is gravely concerned by the ongoing human rights violations against Uyghurs and Muslim minorities in China, as well as by the use of forced labour around the world. This is an important initiative to ensure that importers address their supply chain vulnerabilities and ensure their production promotes out shared Canadian values around the world. Work is underway to fulfill this commitment.

The last three of the Committee's recommendations relate to due diligence and transparency in terms of pension plan investment practices with respect to human rights matters, corruption, and national security.

The Government agrees with the importance of due diligence and transparency regarding pension fund investment decisions. Pension fund managers have a duty to make sound investment decisions and to account for the long-term risks of investments in companies and regions that pose legal, geopolitical, and national security risks and do not take humans rights and corruption seriously. Additionally, governments have a responsibility to ensure that they do this.

The federal and provincial oversight frameworks for Canadian pension plans place an emphasis on due diligence and transparency in terms of plan investment practices. To further strengthen this framework, the Government is developing regulations to meet recent commitments to require federally regulated pension plans to make disclosures related to the consideration of environmental, social, and governance (ESG) factors in investment decisions and the distribution of their investments, both by geographic region and asset-type per region to the Office of the Superintendent of Financial Institutions (OSFI).

On behalf of the Government, I would like to express my appreciation for the efforts of the members of the Committee, witnesses and others who contributed to the valuable

work that led to the preparation of the Report, which, I believe, will provide useful guidance as we continue to improve transparency and oversight of pension fund investment decisions.

Sincerely,

A handwritten signature in black ink, appearing to read 'C Freeland', written in a cursive style.

The Honourable Chrystia Freeland, P.C., M.P.
Deputy Prime Minister and Minister of Finance

ANNEX – DETAILED GOVERNMENT RESPONSE TO EACH RECOMMENDATION

This annex provides the detailed Government response to each of the Committee’s seven recommendations.

Banned Investments (Recommendations 1 to 3)

The Government agrees with the importance of increased scrutiny of pension fund investments and of ensuring that public pension funds do not invest in companies or regions that present national security, corruption, or gross human rights violation risks. Certain companies and regions pose such high risks that they do not present suitable investments for pension plans. The Government’s approach to the oversight of pension funds and to addressing these risks through a variety of tools is aligned with, and demonstrates its commitment to, this objective.

1) That the Government of Canada study how it could compile and maintain an official list of companies deemed unsuitable for investment.

The Government of Canada supports in principle the recommendation to study how it could compile and maintain an official list of companies deemed unsuitable for investment.

The Government of Canada advises pension plans and other investment fund managers with regard to national security considerations so these can be taken into account when exercising due diligence.

Pension plan administrators and investment fund managers also look to other Acts of Parliament in considering these factors. For example, the Government has already listed entities that have been sanctioned for gross and systemic human rights violations including the use of forced labour in the Xinjiang Uyghur Autonomous Region (XUAR) pursuant to the *Special Economic Measures Act*.

Moreover, under the recently enacted Supply Chains Act, certain entities and government institutions are required to report annually and publicly to the Minister of Public Safety on the measures they have taken to prevent and reduce the risk that forced labour or child labour was used by them or in their supply chains.

Pension plan administrators are required by federal or provincial legislation to make prudent investment decisions so that Canadians can retire with dignity. Part of managing the security of pension benefits is the considerations of any risks that could materially

affect the pension fund. This includes considerations such as geopolitical issues or friend-shoring, human rights, governance and environmental risks.

The potential risk that an entity may become subject to Canadian legislation or legislation in other countries would be a factor for pension plan administrators to take into consideration in making investment decisions.

2) That the Government of Canada, in partnership with provinces, study the establishment of a list of companies in the People’s Republic of China that Canadian public pensions plans are prohibited from investing in due to risks to national security, corruption or gross human rights violations.

The Government of Canada supports in principle the recommendation to, in partnership with provinces, study the establishment of a list of companies in the People’s Republic of China that Canadian public pensions plans are prohibited from investing in due to risks to national security, corruption or gross human rights violations.

Canada is deeply concerned by the ongoing human rights violations against Uyghurs and Muslim minorities in China and the use of forced labour around the world. The Government of Canada remains committed to promoting responsible business conduct and human rights globally and ensuring that Canada, including Canadian businesses, is not complicit in human rights violations. The Government has demonstrated this commitment through its public support of the UN Office of the High Commissioner for Human Rights’ 2022 assessment of human rights in Xinjiang, calling on China to respond to the recommendations in the report, as well as supporting the recent enactment of the Supply Chains Act, which considers forced and child labour globally.

In cases where credible and verifiable information is available with respect to foreign entities engaged in or complicit with human rights violations, Canada is able to apply sanctions under SEMA. In 2021, Canada sanctioned four PRC individuals and one entity for their role in gross and systemic human rights violations in the XUAR of China. Should compelling evidence emerge that a PRC firm is making use of forced labour or implicated in other gross and systematic human rights violations, including that of Uyghur Muslims from the XUAR, those firms could be added to the existing schedule barring Canadians or Canadian firms from any economic or financial activity with these entities.

The Government of Canada also advises pension plans and other investment fund managers with regard to national security considerations so these can be taken into account when exercising due diligence.

3) That the Government of Canada work with the United States and other allies to develop common approaches to human rights implications of public pension plan fund investments, including developing a list of banned investments because of suspected human rights abuses.

The Government of Canada supports in principle the recommendation to work with the United States and other allies to develop common approaches to human rights implications of public pension plan fund investments, including developing a list of banned investments because of suspected human rights abuses.

Consistent with Canadian values, Canada must continue to work to end human rights violations. International cooperation is necessary to promote human rights globally and the Government of Canada regularly consults and shares information with allies on a range of subjects of mutual concern, including human rights.

Moreover, the Government works with other international partners in coordinating responses to human rights violations, leveraging available legal and regulatory instruments and sharing information as well as best practices. For example, in 2023 Canada supported a joint statement at the UN Third Committee, issued on behalf of 50 countries that expressed concern about the human rights situation in the PRC, especially the human rights violations of Uyghurs and other predominantly Muslim minorities in the XUAR. Additionally, concerns over human rights abuses abroad by Canadian companies in the garment, mining and oil and gas sectors can be submitted to the Canadian Ombudsperson for Responsible Enterprise (CORE).

Supply Chains and Imports (Recommendation 4)

4) That the Government of Canada, in accordance with its commitment in Budget 2023, by 2024, propose legislative changes and enhanced enforcement to eliminate forced labour from Canadian supply chains and to reinforce the prohibition on the import of goods produced by forced labour.

The Government of Canada supports in principle the recommendation to, in accordance with its commitment in Budget 2023, by 2024, propose legislative changes and enhanced enforcement to eliminate forced labour from Canadian supply chains and to reinforce the prohibition on the import of goods produced by forced labour.

The Government is gravely concerned by the human rights violations against Uyghurs and Muslim minorities in China and the use of forced labour around the world. The Government remains committed to introducing strong, effective and enforceable due diligence legislation in 2024 to address forced labour in Canadian supply chains, in accordance with the Minister of Labour and Seniors' shared mandate letter commitment

and the Budget 2023 announcement. Furthermore, beyond supply chain legislation, the Government is also committed to bringing forward measures to strengthen the import prohibition on goods produced using forced labour, as referenced in Budget 2023. These are important initiatives to ensure that importers address their supply chain vulnerabilities and ensure their production promotes our shared Canadian values around the world.

In order to advance this work, the Labour Program of Employment and Social Development Canada and other key federal departments hosted a technical roundtable with a variety of stakeholders (including civil society organizations, labour organizations, industry representatives and academics) in October 2023. The purpose of this roundtable was to discuss aspects of government-led supply chain legislation, such as potential due diligence obligations, the entities to be regulated, and means of strengthening the import prohibition. The responses received from this engagement, as well as previous consultations on labour exploitation in global supply chains held in 2019 and 2022, will help inform the development of the government's proposals.

In addition to these commitments, work continues on a number of other initiatives to tackle exploitation in Canadian supply chains. These include the inclusion of comprehensive and enforceable provisions on forced labour and child labour in Canada's free trade agreements, the 2022 introduction of an enhanced Responsible Business Conduct Abroad Strategy to promote and increase corporate due diligence when doing business abroad, and the strengthened federal procurement contracting regime that establishes expectations for suppliers and sub-contractors on upholding human and labour rights.

The Government will continue to work closely with stakeholders and international partners to improve the overall approach to addressing these issues.

Transparency and Reporting (Recommendations 5 to 7)

The Government agrees with the importance of due diligence and transparency regarding pension fund investment decisions. Pension fund managers have a duty to make sound investment decisions and to account for the long-term risks of investments in companies and regions that pose legal, geopolitical, national security risks or do not take human rights and corruption seriously. Additionally, governments have a responsibility to ensure that they do this.

The Canada Pension Plan Investment Board (CPPIB) was set up by the federal and provincial governments to prudently invest surplus Canada Pension Plan (CPP) funds. It was given a clear mandate and a unique governance structure in its enabling legislation. CPPIB's legislative objective is to maximize returns without undue risk of loss and to manage amounts transferred to it in the best interests of CPP contributors and beneficiaries. Its governance structure was designed to allow CPPIB to operate independently and in the best interest of contributors and beneficiaries, while being accountable to the federal and provincial governments that serve as stewards of the CPP.

The Public Sector Pension Investment Board (PSPIB) was set up by the federal government to manage the investments of the statutory pension plans for the federal public service, Royal Canadian Mounted Police, and the Canadian Armed Forces (Regular Force and Reserve Force). Similar to the CPPIB, it was given a clear, distinct mandate and a unique governance structure in its enabling legislation.

The federal government is solely responsible for federally regulated private sector pension plans (seven per cent of plans in Canada). Federally regulated private sector pension plans include those linked to federally regulated areas of employment (e.g., banking, telecommunications, interprovincial transportation), private pension plans in the Territories, and in certain federal Crown corporations. Most pension plans (93 per cent) are the responsibility of provincial governments. This includes six of Canada's eight largest pension funds.

5) That the Government of Canada mandate through legislation that federally regulated public pension plans conduct and report enhanced due diligence for all investments in authoritarian states, enforce penalties for non-compliance, and consult with provinces on harmonizing that approach.

The Government of Canada supports in principle the recommendation to mandate through legislation that federally regulated public pension plans conduct and report enhanced due diligence for all investments in authoritarian states, enforce penalties for non-compliance, and consult with provinces on harmonizing that approach.

To further strengthen this framework and to improve transparency, the Government is developing regulations to meet recent commitments to require federally regulated pension plans to make disclosures related to the consideration of ESG factors in investment decisions, the distribution of their investments, both by region and asset-type per region, and their crypto asset holdings to OSFI.

The Government believes that due diligence and transparency are important aspects of pension plan investment decisions. Pension fund managers have a duty, in investing plan assets, to account for the long-term risks of investments in companies and regions that pose legal, geopolitical, national security risks or do not take human rights and corruption seriously.

Pension plans in Canada have diverse investment portfolios and there are no restrictions on the types of investments that plan administrators can make. They are required to set out their investment plans in a Statement of Investment Policies and Procedures. Both the Canadian Association of Pension Supervisory Authorities (CAPSA) and OSFI provide significant guidance on expectations regarding investment decisions by pension plans. This guidance emphasizes the importance of clearly identifying investment risk. It also emphasizes the importance of due diligence when considering investments, which includes carrying out an independent and thorough investigation to determine the advantages and disadvantages of a particular investment. Plan beneficiaries have the ability to request this information from their plan administrator.

6) That the Government of Canada request that pension plan regulators, including OSFI and provincial counterparts, consider creating a standardized transparency reporting regime for pension plans and institutional investors for active and passive investments.

The Government of Canada supports in principle the recommendation to request that pension plan regulators, including OSFI and provincial counterparts, consider creating a standardized transparency reporting regime for pension plans and institutional investors for active and passive investments.

The Government recognizes the importance of transparency regarding pension plan investments. Pension fund managers have a duty to take into account the risks of investments in companies and regions that pose legal, geopolitical, and national security risks. The Government is taking action aligned with this recommendation.

To improve transparency around pension investments, the 2023 *Fall Economic Statement* announced that the Government has proposed to require large federally regulated pension plans to disclose the distribution of their investments, both by jurisdiction and asset-type per jurisdiction, to OSFI. This information will be made publicly available, and the Government will engage with provinces and territories to discuss similar disclosures by Canada's largest pension plans in a simple and uniform format. Having comparable information about the distribution of large pension plans' assets by jurisdiction and by asset-type would help to provide a more comprehensive picture of the overall diversity of their plan assets, including their allocation to different regions.

7) That the Government of Canada requests that pension plan regulators, including OSFI, establish a code of ethics to guide the investment practices of federal Crown corporations responsible for investing public pension funds, with due consideration of human rights matters, corruption, and national security.

The Government of Canada supports in principle the recommendation to request that pension plan regulators, including OSFI, establish a code of ethics to guide the investment practices of federal Crown corporations responsible for investing public pension funds, with due consideration of human rights matters, corruption, and national security.

Domestic and international stakeholders widely agree that the obligation of pension plan administrators to make prudent investment decisions is well aligned with the consideration of ESG factors, and many have adopted either voluntary or mandatory standards for disclosures. The plan administrator is also responsible for providing information to members and prudently managing the pension fund.

With respect to federally regulated pension plans, in Budget 2022 the Government committed to requiring federally regulated pension plans to improve governance and administration and make disclosures related to ESG to OSFI. In fall 2023, the Department of Finance Canada consulted with several stakeholders, including provinces, on proposed regulatory amendments related to governance policies and ESG disclosures. The Department is assessing these comments and is working to bring forward in the coming months the regulatory amendments specifying the disclosure requirements with respect to governance and ESG considerations. This will improve transparency regarding investment decision-making processes.

CAPSA, the national association of pension regulators, released a revised draft principles-based guideline in May 2023, on establishing good risk management, including ESG considerations. These draft guidelines note that pension administrators should consider whether any particular ESG factors are relevant to investment performance and take appropriate action based on that determination. The draft guidelines also note that, consistent with their fiduciary duty, plan administrators may use ESG information as a deciding factor when making investment decisions.

The CPPIB and the PSPIB apply leading investment practices by taking ESG risks and opportunities fully into account. Among their due diligence procedures, when investing, the CPPIB and PSPIB incorporate aspects of human rights into their investment decision-making processes, consider political, legal and regulatory risks, and use tools and systems to monitor and evaluate passive and active holdings.