Principles for Responsible Investing

Contents

1. Introduction

Responsibility and sustainability requirements are part of VER's investment decision-making and VER should not promote unsustainable or irresponsible economic activity. VER's investment activities are based on the Act on the State Pension Fund and its requirements, as well as on guidelines issued by the Ministry of Finance.

Environmental, Social and Governance (ESG) requirements need to be considered as part of the assessment of risks and opportunities. By pursuing responsible and sustainable investing, VER aims to improve the risk-return ratio of its investments by reducing risk and exploiting the opportunities offered by the transition to sustainability. Investment decisions are based on VER's return requirement and the performance potential of the investments with due regard to risk levels and sustainability requirements. Consideration of responsibility and sustainability in VER's investment decisions must not be at variance with the requirements for investment activities laid down by law.

The purpose of VER's Principles for Responsible Investing is to define VER's objectives for responsible investment and the means available to achieve them. While VER's Principles for Responsible Investing cover all asset classes, their application varies according to asset class and method of investment. The Principles for Responsible Investing contribute to an understanding of responsible investment choices and approaches, increasing the openness and transparency of investment activities.

VER's long-term investment policy is determined by VER's Board of Directors. The Board decides on VER's Principles for Responsible Investing, and VER's policy and objectives are assessed and updated as needed.

VER's executive management determines the execution policies serving as a basis for issuing instructions and developing practical procedures for portfolio management. Portfolio managers monitor the sustainability performance of their portfolios implementing VER's Principles for Responsible Investment.

VER monitors and reports on the carbon footprint of investments. The first carbon footprint targets were set in 2019. In 2020, the Council of State adopted a road map for achieving the goal of carbon neutrality and in that context instructed VER regarding the theme of sustainability. The guidelines are currently also incorporated into VER's operational directive. VER determined the carbon footprint of its investment activities in 2020 and clarified its sustainability objectives to reduce its carbon footprint in autumn 2022.

2. Principles for Responsible Investing and Climate Views

VER's Principles for Responsible Investing forms the basis for VER's responsible investment activities and guides the setting of sustainability objectives. They cover all asset classes, but their application depends on the characteristics of each asset class.

At VER, responsible investment rests on the following principles:

1. VER believes that attention to essential ESG[1] factors has a positive impact on the long-term performance of the investment portfolio. Consideration of ESG risks and opportunities, or ESG integration, is an inherent part of a long-term investor's process.
2. VER wants to promote transparency in its investees and their sustainability activities.
3. VER requires that the investees act responsibly and, in particular, give due consideration to climate change in their operations, and VER's investees should not obstruct sustainable development.
4. The goals of VER's climate actions are to manage the financial risks to the portfolio from climate change and support the implementation of the Paris Climate Agreement.[2]

Climate change causes uncertainty in the future investment environment. VER's climate views are intended to serve as long-term guidelines for managing VER's climate risk and directing investments towards assets that promote the green transition. At the same time, they guide the setting of VER's climate goals.

VER's climate views are as follows:

1. Climate change is a serious threat to humanity and mitigating it will mean a significant reduction in emissions, which will require a transition towards a low-carbon economy (the so-called green transition).
2. To make the green transition a reality, governments, businesses and investors must commit to the Paris Climate Agreement.
3. A climate strategy that focuses only on exclusion can be detrimental to the green transition and increases the proportion of active risk in the portfolio. Often a better option is to integrate relevant climate risks and opportunities into investment decisions, invest in climate solutions and transitioning assets, and influence carbon-intensive investments.

3. Sustainability goals

The fund's long-term return depends on sustainable economic growth and functioning financial markets. When choosing investments, VER must take sustainable development into account and avoid investments that slow down sustainable development. Therefore, the goal of VER's responsible investment activities is to identify long-term sustainability risks, manage them and support sustainable development by allocating capital and engaging in dialogue with investees.

1. Climate goals

To contribute to the targets of the Paris Climate Agreement and manage the portfolio's climate risks, VER has set the following goals:

[1] ESG stands for Environmental, Social and Governance.
[2] As part of the State of Finland, VER is committed to the Paris Climate Agreement, which aims to keep the global average temperature increase well below 2 degrees Celsius compared to pre-industrial levels and to strive for measures to limit warming to less than 1.5 degrees Celsius.

- VER aims for the carbon neutrality of the entire portfolio in 2050.[3] The timeframe of the goal was chosen in view of the globally dispersed nature of VER's portfolio and the geographical diversity of each country's carbon neutrality goals.
- The carbon intensity reduction goal for VER's listed portfolio for 2025 is 30% compared to the 2019 level[4], and the emission reduction goal for 2030 is 50%.
- With regard to liquid corporate bonds, VER's goal is to keep the carbon intensity of the portfolio below the benchmark index.

VER will reduce the carbon footprint of its portfolio by index-driven investing. Currently, however, major market indices are not in line with the Paris Climate Agreement, which poses challenges to the emission reduction targets of a globally diversified portfolio. The achievement of VER's emission reduction targets is therefore dependent on the emission reduction efforts of governments and companies. This is why VER monitors the carbon neutrality schedules set by governments and companies and their implementation. VER aims to use the emission reduction targets adopted by the Science-Based Targets initiative (SBTi) to identify and weigh portfolio companies aiming for carbon neutrality. The aim is to get more and more listed companies to commit to the Paris Climate Agreement. During 2023, VER has analysed the SBT coverage of direct investments in the listed equity portfolio. In the coming years, VER will assess its applicability as a climate goal. For alternative illiquid fund investments, VER tracks emissions taking into account the characteristics of each asset class. VER aims to harmonise emissions reporting over time.

2. UN Global Compact

The UN Global Compact is the UN's corporate responsibility initiative to promote and develop the environmental, social and economic sustainability of companies and communities. The ten principles of the initiative (Appendix 2) are based on the following universal principles:

1. UN Universal Declaration of Human Rights
2. ILO Declaration on Basic Principles and Rights at Work
3. UN Rio Declaration on Environment and Development
4. UN Convention against Corruption

VER monitors the implementation of the Global Compact principles with the help of an external service provider. VER aims to ensure that none of its portfolio companies violate the Global Compact principles. In the event of a potential breach of norms, VER's portfolio management team will analyse the case and report it to VER's internal Risk Management Committee, which will decide on the future of the investment. Repeated major breaches of norms can lead to the sale of the asset.

[3] Currently, the portfolio's carbon footprint can be measured in listed shares and liquid corporate bonds. We expect this to extend to government bonds and unlisted assets in the coming years.

[4] Emissions known on 31 December 2019.

4. Responsible Investment Approaches

VER signed the United Nations Principles for Responsible Investment (UN PRI) in 2011. These principles have evolved globally as a basis for best practices in responsible investing, and they also steer the development of VER's responsible investment processes. A UN PRI signatory seeks to:

1. Include the ESG review as part of the investment process.
2. Act as an active owner and incorporate ESG issues in its owner policies.
3. Promote ESG reporting on its investments.
4. Promote the adoption of responsible investment principles in the investment industry.
5. Promote responsible investment practices in cooperation with other investors.
6. Report on its activities and progress made in responsible investment.

VER's Principles for Responsible Investing cover both internally and externally managed assets for all asset classes. Regarding new fund investments, VER will review the fund's ESG processes, personnel and metrics. VER assesses the sustainable investment performance of external fund managers through an ESG questionnaire and a dialogue with the fund management company. VER is aware that external managers approach ESG integration in different ways and that their climate goals vary. VER expects that in the next few years more and more funds will set ambitious climate goals and analyse ESG risks and opportunities as part of their daily investment activities.

VER divides responsible investment into three levels. The first level is investing in line with values and international norms, aiming to meet certain quality requirements in terms of sustainability. For institutional investors, there is a reputational risk in investing in non-compliant or unsustainable assets such as coal. The second level is ESG integration, through which VER aims to analyse changes in ESG issues. The third level is impact, which VER seeks to achieve primarily through dialogue with companies and asset managers. VER can also achieve impact through investments.

1. Investing in line with values and international norms

Investors often approach this level of sustainability through exclusion. According to Finsif, the purpose of exclusion is to avoid investing in products, countries, industries or companies whose practices are considered unsustainable. VER's exclusion criteria are based on ethical exclusion, where an investee is excluded from the investment universe because of its product or behaviour. As regards fund investments, VER follows the exclusion list below, where applicable.

In the case of product-based exclusion, the investee is excluded if its product is inherently harmful to humans or the environment. Another VER criterion is that there should be no negative impact if the product is removed from the world. Based on these criteria, VER does not make direct investments in companies with more than 10% of their turnover coming from the following businesses:

- Tobacco
- Controversial weapons

- Coal

Under behavioural exclusion, VER excludes companies that violate international norms. Monitoring is done through a norm screening report produced by an external service provider. In addition, the investment should meet VER's expectations as described in VER's Ownership Policy.

Public services are financed through tax revenue. Aggressive tax planning weakens the ability of the public sector to collect tax revenues. The assessment of tax liability is particularly relevant for illiquid investments. VER follows evaluations by international organisations (such as the EU and OECD). VER does not invest in countries on the EU's blacklist, nor does VER invest in funds established in these countries.

2. ESG integration

According to Finsif, ESG integration refers to the systematic use of ESG data in investment analysis and decision-making. ESG integration often focuses on economically relevant ESG factors, which vary from sector to sector. For example, in manufacturing, greenhouse gas emissions and occupational safety are key ESG factors, while in healthcare, customer safety and information security may affect the value of a company operating in the sector.

In direct equity and fixed income investments, portfolio managers take ESG factors into account as part of their investment analysis and ongoing monitoring of investments. In VER's fund investments, the level of ESG integration may vary, because in passive fund investments, VER cannot influence the fund's objectives. Part of VER's passive fund investments leverage ESG indices produced by an external service provider, where sustainability risk management affects the content and weights of the index. In the case of active fund investments, VER can choose a fund that meets VER's sustainability objectives. In the case of illiquid fund investments, VER's portfolio management ensures a sufficient level of ESG integration before an investment decision is made.

3. Active ownership

VER seeks to achieve impact first and foremost through active ownership. Active ownership refers to investor processes in which the investor uses their ownership rights to promote more sustainable business practices and to secure investment returns. VER's portfolio managers regularly discuss sustainability issues with both portfolio companies and external fund managers. VER's Ownership Policy describes the expectations for the sustainable operation of portfolio companies and external asset managers.

In addition to active ownership, VER seeks to impact through its investment portfolio. At the beginning of 2024, a new ESG transition portfolio consisting of global active funds was added to VER's portfolio. The aim of the funds is to change the way companies operate through the exercise of influence, and in doing so to influence their carbon emissions, among other things. VER also looks at ways to increase the positive effects of the portfolio and reduce its negative effects.

5. Monitoring and Reporting

VER promotes the transparency of its own activities. VER reports on the activities and results of responsible investing internally and externally and conducts a continuous dialogue with the management of its portfolio companies and its fund managers. VER uses an external service provider to screen the portfolio for potential non-compliance and controversial weapons. VER monitors known breaches and suspicions and takes them into account when making investment decisions. VER reports to the Board on the implementation of principles and objectives. The results of VER's PRI report are presented to the Board annually. In addition, VER must provide the Ministry of Finance once a year with information on the sustainability and carbon footprint of its investment activities and a statement issued by its Investment Consultative Committee. Reporting is carried out in a manner agreed with the Ministry of Finance.

VER publishes annual reports on the carbon footprint of the portfolio, i.e. the carbon intensity of the portfolio and the absolute emissions of the portfolio regarding listed shares and corporate bonds. VER published its first climate report in spring 2022.

Appendix 1: Glossary

Externality	Externality is a term in economics used to refer to the consequences of an action on parties not taken into account by the actor.
TCFD (Task Force on Climate-Related Financial Disclosures)	TCFD is an international reporting recommendation that focuses on the threats and opportunities of climate change.
SBTi (Science Based Targets initiative)	The Science Based Targets initiative (SBTi) is a collaborative initiative of CDP, UN Global Compact, WWF and WRI, which advocates ambitious climate action to reduce emissions in the private sector in line with the Paris Climate Agreement.
Finsif	Finsif is a Finnish association for responsible investing, which aims to promote responsible investing in Finland.
Carbon intensity (TCFD)	The carbon intensity of the portfolio is the carbon intensity weighted by the portfolio weights (tonnes CO2e / turnover mUSD).

Appendix 2: Global Compact principles[5]:

1. Businesses should support and respect universal human rights within their sphere of influence.
2. Businesses should ensure that they are not complicit in human rights abuses.
3. Businesses should uphold freedom of association and effective recognition of the right to collective bargaining.
4. Businesses should support the elimination of all forms of forced labour.
5. Businesses should support the effective elimination of child labour.
6. Businesses should support the elimination of discrimination in respect of employment and occupation.
7. Businesses should support a precautionary approach to environmental challenges.
8. Businesses should undertake initiatives to promote greater environmental responsibility.
9. Businesses should encourage the development and diffusion of environmentally friendly technologies.
10. Businesses should work against corruption in all its forms, including extortion and bribery.

[5] https://www.globalcompact.fi/kymmenen-periaatetta