

Church Pension Fund's Guidelines for Responsible Investing

Approved by the Board of the Church Pension Fund on 3 October 2018

Content

| | |
|--|----|
| 1 Introduction..... | 3 |
| 2 The Church Pension Fund as an investor..... | 3 |
| 3 The Principles of Responsible Investment as a framework..... | 5 |
| 4 Responsible companies as investment objects | 6 |
| 5 Approaches to responsible investing | 8 |
| 5.1 Responsibility analysis | 8 |
| 5.2 Active ownership and engagement | 9 |
| Direct engagement..... | 9 |
| Indirect engagement..... | 10 |
| 5.3 Impact investing..... | 11 |
| 6 Selection and monitoring of asset managers | 12 |
| 7 Responsible investing in practice | 14 |
| 7.1 Equity investments..... | 14 |
| 7.2 Fixed-income investments | 15 |
| 7.3 Alternative investments..... | 15 |
| 8 Reporting | 18 |
| 9 Decision-making process | 19 |

1 Introduction

The Church Pension Fund is committed to responsible investing. Responsible investing is an effective way to ensure a good return on investments and the management of investment risks. The Pension Fund stresses the importance of taking ESG (Environment, Social and Governance) issues into account in all investment activities.

Responsible investing is becoming increasingly mainstream both in Finland and on the international level. The Church Pension Fund wants to be actively involved in the process of advancing awareness about responsible investing by operating openly, sharing information in various forums and working together with other investors. These guidelines are intended to provide an outline for the Pension Fund's responsible investment activities, and to clarify the Pension Fund's expectations for asset managers and companies.

The Church Pension Fund's guidelines for responsible investing are primarily applicable to the investment activities of the Pension Fund. The guidelines shall also serve as an example for parishes and other investment entities within the sphere of the Evangelical Lutheran Church of Finland. The guidelines were previously updated by the Church Pension Fund in 2014. In December 2016, the Church Pension Fund published a separate Climate Change Strategy.

The ethical values of the Church serve as the foundation for the responsible investment activities of the Church Pension Fund. The Pension Fund focuses particularly on favouring responsible investment objects and influencing corporate behaviour. The selection of asset managers and development of this co-operation are key aspects of the Pension Fund's responsible investment activities.

The guidelines for responsible investing were approved by the Board of the Church Pension Fund on 3 October 2018. The guideline update was carried out by the Responsible Investment Work Group appointed by the Board. The guidelines will be updated as necessary, and the Board will monitor the development of the activities by publishing an annual report on responsible investing. Additionally, the Pension Fund includes its objectives for responsible investments in its annual investment plan.

2 The Church Pension Fund as an investor

The task of the Church Pension Fund is to secure the payment of pensions to Church employees and to balance the future development of the pension contributions paid by parishes. Established in 1991, the Pension Fund gains its assets from pension contributions and investment incomes. As of 2016, the Pension Fund has paid out more pensions than the Fund has gathered as pension contributions, so part of the pensions has been financed by the Fund's investment returns. The pension security of employees of the Evangelical Lutheran Church of Finland is prescribed by the Public Sector Pensions Act.

Church Pension Fund investments

The Church Pension Fund's investments are handled by the Investment Unit, whose activities are overseen by the Board of the Pension Fund. As with other pension investors, the Pension Fund is a long-term investor, whose investments may experience significant value changes over the short term. Despite the long investment period, the Pension Fund must continuously maintain sufficient control of all investment risks. The investments must be consistently allocated to different asset categories, geographical regions, sectors, asset managers and investment styles.

As determined by the strategy, the Pension Fund's long-term real profit target is 3.5 per cent with a 9.5 per cent risk level. The Pension Fund has distributed its investments to listed equity, fixed-income and alternative investments.

The Pension Fund primarily uses investment funds in its investment activities. The task of the Pension Fund's Investment Unit is to select successful, responsible funds and asset managers to serve as co-operative partners and to collaborate with them in order to ensure compliance with the investment principles while developing the related activities. The Pension Fund can also utilise the services of external experts to screen the responsibility of its portfolio and to assist in its engagement activities.

Values and ethics

The values listed in the Strategy of the National Church Council are reflected in the basic task of the Church Pension Fund to manage pension assets profitably, securely and responsibly. The Investment Unit shall respond openly to all questions put forth by the personnel, pension recipients, parishes and the media. In its role as a public actor, the Pension Fund feels it is important to ensure that its investment activities are transparent and fair. The Investment Unit complies with the guidelines for responsible investing and the UN supported Principles for Responsible Investment (PRI).

Lutheran ethics are based on the Golden Rule of humanity, which is accepted worldwide. It is expressed in the words of Jesus as written in the Gospel of Matthew: "Therefore, whatever you want men to do to you, do also to them, for this is the Law and the Prophets," (Matthew 7:12). When God created man, he instilled in him the knowledge of how we should treat one another. The act of putting the Golden Rule into practice is not a straightforward process, but rather its application involves stepping into the shoes of another person or group and attempting to discover what would be truly good for them from their own perspective. As an owner and investor, the Church Pension Fund takes into account its key stakeholders, namely those affected by investment policies, and considers the realisation of their benefit.

3 The Principles of Responsible Investment as a framework

The Church Pension Fund's responsible investment principles are at the core of its investment activities. As of 2008, the Pension Fund has undertaken to comply with the UN supported Principles for Responsible Investment and has built its responsible investment activities around these principles. The PRI helps the Pension Fund to carry out responsible investment activities.

As a signatory of the Principles for Responsible Investment (PRI), the Church Pension Fund has committed to the following:



- 1. We will incorporate ESG issues into investment analysis and decision-making processes.**
 - We draw up an annual responsible investment plan, which includes the goals for responsible investment.
 - A separate Climate Change Strategy guide our climate change work.
 - All members of the Pension Fund team work on developing responsible investment activities within their own area of responsibility.
 - We apply ESG criteria to our selection of asset managers.
 - We only work with asset managers who have committed to the Principles of Responsible Investment.
- 2. We will be active owners and incorporate ESG issues into our ownership policies and practices.**
 - We have principles of active ownership and engagement that steer our ownership practices and engagement activities.
 - We engage in continuous dialogue about responsible business activities with domestic and foreign companies.
 - We participate in the annual general meetings of domestic companies.
 - We regularly monitor the content of our investment portfolio and any possible norm violations.
- 3. We will seek appropriate disclosure on ESG issues by the entities in which we invest.**
 - We support investor initiatives that aim to promote the responsible reporting practices of companies.
 - We continuously monitor the development of the responsible investment activities of our asset managers and encourage them to report on the ESG impacts of their investment activities.
- 4. We promote the acceptance and implementation of the Principles within the investment industry.**
 - We raise ESG issues at the request for tender phase and favour asset managers that comply with the Principles.
 - We participate in relevant seminars and hold lectures on responsible investing for other investors and students.
 - We keep information on responsible investments updated on our website.
- 5. We will work together to enhance our effectiveness in implementing the Principles.**
 - We actively participate in the activities of Finsif and implement the Principles.
 - We collaborate with other investors and encourage them to invest responsibly.
 - We share information with the parishes and maintain regular contact with other investors within Church organisations.
- 6. We will report on our activities and progress towards implementing the Principles.**
 - We include an ESG assessment to the monthly and annual monitoring of our investment funds.
 - We publish an annual report on responsible investments.
 - We report on the carbon footprint of our equity and fixed-income investments.
 - We report to PRI, on an annual basis, on the progress of the implementation of the Principles.

4 Responsible companies as investment objects

Through its investment activities, the Church Pension Fund wants to advance responsible business practices and the success of responsible companies. The following operational policies describe the Pension Fund's view of corporate responsibility:

Compliance with laws and international norms is the minimum requirement for corporate responsibility. The Church Pension Fund recommends that companies commit to the *UN's Global Compact* initiative and comply with the *OECD Guidelines for Multinational Enterprises*. Corporate responsibility forerunners exceed the requirements of the norms and laws and create a foundation for future standards.

Positive influence. In their use of natural resources, responsible companies consider the needs and rights of future generations and consciously minimise the harmful impacts of their operations on the environment and society at large. Forerunner companies harness market forces to create solutions for the challenges of sustainable development.

Focusing on stakeholders. A company that is acting responsibly incorporates the expectations of its stakeholders into its own activities and business development. The basis for corporate responsibility is an understanding that the company has other tasks and obligations in society besides making a profit for the shareholders. Stakeholder-based management involves the perspectives of all stakeholders, as this is considered to be beneficial, in the long term, for the shareholders as well. The company is responsible for the positive as well as the negative impacts of its operations on those communities in which it operates. This means that the company is responsible for the activities of its co-operative partners as well as its network of subcontractors.

Commitment of management. Corporate responsibility relies on a strategy in which responsibility is incorporated into the company's management system and, through that, into the operational guidelines, job descriptions and, when necessary, profit steering and bonus systems. The commitment of the Board and top management is essential in order for the responsibility to penetrate the entire organisation. Training and internal communications ensure that the entire personnel is familiar with and recognises the requirements for responsible practices within the company and their own jobs.

Climate change. Climate change is a global phenomenon that will have an unavoidable impact on the world's societies and businesses in the future. In order to slow climate change, companies will have to reduce the generation of greenhouse gases in the atmosphere. Responsible companies prepare in advance for the risks and possibilities brought on by climate change and include the related actions into their overall strategy.

Fiscal responsibility. A responsible company complies with legislation and its objectives when carrying out tax planning. The Church Pension Fund views it as important that tax payments reflect a company's financial activities and that taxes should be paid within the different countries of operation in accordance with the actual activities taking place there.

Open communications. Corporate responsibility is credible if the company can prove that the requirements for responsibility have led to actual strategic changes. Words complement deeds: transparency and communications that meet the needs of the interest groups create trust. A company's ability to hold tight to its values, correct its operations as needed and anticipate the risks related to the social, environmental and political conditions indicates good corporate governance and management practices.

Reporting. An investor needs reliable and comparative information about companies in order to make informed investment decisions. The Church Pension Fund recommends that companies report to the Carbon Disclosure Project any measures they have taken to reduce the impact of their operations on climate change. Furthermore, companies are encouraged to report on their activities in accordance with the Global Reporting Initiative (GRI). The concept of open communications also includes the reporting of a company's tax policies and tax footprint.

5 Approaches to responsible investing

The Church Pension Fund applies several different approaches to responsible investing and combines them in different ways. The different approaches to responsible investing are not mutually exclusive, but rather look at the issue from different angles. In the case of the Pension Fund, the use of approach depends on the asset category in question and whether the investment is direct or indirect. The responsible investment approaches of the Pension Fund include responsibility analysis, active ownership and engagement, and impact investing.

| | RESPONSIBILITY ANALYSIS | | | | ACTIVE OWNERSHIP | | IMPACT INVESTING |
|---------------------------|-------------------------|-----------------|----------------------|-----------|------------------------|--------------------------------------|------------------|
| | Norm-based screening | ESG-integration | Sustainability theme | Exclusion | Engagement discussions | Annual General Meeting participation | Impact investing |
| Direct equity investments | ● | ● | | ● | ● | ● | |
| Equity funds | ● | ● | ● | ● | ● | ● | |
| Fixed-income funds | ● | ● | | ● | ● | | ● |
| Alternative investments | | ● | ● | ● | ● | | ● |

Figure: A summary of the Church Pension Fund’s responsible investment approaches and their application within the different asset classes. A mark signifies that the approach in question is being applied to the specific asset class. The use and form of different approach methods vary by fund type.

5.1 Responsibility analysis

The responsibility analysis is used to assess the level of responsibility of investment objects in terms of the different ESG criteria, and this information can then be used to either favour or avoid the companies in question. The working methods used in the responsibility analysis vary according to the fund in question. The following are a few examples of different methods:

Norm-based screening. The investor assesses the responsibility level of specific companies through their compliance with the UN and OECD international norms. These norms deal with, among other areas, UN agreements on human rights, labour laws, corruption and environmental protection. The Pension Fund regularly carries out a norm-based screening of its portfolio. If any violations are discovered, an engagement process is initiated.

ESG integration. The investor integrates ESG issues into the investment analyses along with traditional economic indicators. The Pension Fund favours asset managers that actively monitor the ESG issues in companies as part of their investment activities and strive to understand the impacts of ESG issues on a company’s potential profits and risks.

Thematic investing. The investor favours companies within a specific sector or companies that offer products or services that support sustainable development. The Pension Fund focuses on sustainable development

themes that include climate change, forests, renewable forms of energy and changes brought on by demographic change in society.

Exclusion of companies. The investor excludes from the investment universe any companies that provide products and services that are determined to be controversial or unethical in nature. The Pension Fund avoids direct investments in companies that manufacture alcohol, tobacco or weapons or provide gambling services, adult entertainment or fossil fuels.

5.2 Active ownership and engagement

In engagement with companies, the Church Pension Fund wants to bear responsibility as an owner by promoting responsible business practices, thereby ensuring long-term value for its investment objects. In order for this to be possible, companies must act persistently and manage risks in the interest of their shareholders.

The Pension Fund initiates a dialogue with a company in order to change corporate practices. Divesting from a security rarely leads to changes in company practices, and in such a case, the investor also forfeits all rights of ownership. If the engagement dialogue has proven unsuccessful, the decision can be made to divest.

The Pension Fund is involved in both *direct* and *indirect* engagement. In direct engagement, the Pension Fund attends annual general meetings and participates in company dialogue. In indirect engagement, an asset manager or consultant carries out the dialogue with the companies and participates in the annual general meetings on behalf of the Pension Fund. Direct engagement is primarily used with domestic companies, since the close proximity makes it easier to connect for discussions. The Pension Fund uses external experts to carry out its engagement on the international level.

Direct engagement

A representative of the Church Pension Fund can utilise voting rights in the annual general meetings of companies or enter into dialogue with company representatives at corporate events or seminars.

Participation in annual general meetings. The Pension Fund participates in the annual general meetings of domestic listed companies in co-operation with its asset managers. The Pension Fund annually negotiates with the asset managers regarding the upcoming general annual meeting season and related themes. The Pension Fund has drafted separate guidelines for the annual meeting representative. A report covering the most critical observations shall be drafted at the end of the general meeting season.

The Church Pension Fund bases its ownership practices on the *OECD Principles of Corporate Governance (2015)*. The Church Pension Fund also endorses the *Finnish Corporate Governance Code*, which was approved on 1 October 2015, and recommends that non-listed companies comply, as applicable, with the principles as well.

The Church Pension Fund would particularly like to emphasise the following aspects in its ownership steering:

- moderation in company management and Board remuneration
- board diversity and sufficiency of resources
- long-term personnel policy
- a public, predictable dividend policy

- transparent and comprehensive reporting on financial and responsibility issues.

The Church Pension Fund encourages companies to observe good annual meeting practices. This refers to, among other things, the presentation of clear grounds for the content of the agenda well in advance of the annual meeting date.

Meetings with company representatives. Personal meetings with company management or other representatives provide a good foundation for dialogue in a way that is not possible within the context of annual general meetings. The Pension Fund can participate in such meetings together with a consultant, asset managers or other owners. Dialogue can also be initiated with companies by organising seminars and other events.

Indirect engagement

The indirect engagement of the Church Pension Fund involves the selection of international engagement cases, theme-specific proactive engagement and participation in investor initiatives.

Selection of international engagement cases. The Pension Fund reviews all of its equity and fixed-income investments biannually to generate a current overall picture of the content of the investment portfolio. With the help of an external screening and engagement service, the Pension Fund is able to identify, within its own investment portfolio, international norm violations concerning UN conventions related to human rights, labour law, anti-corruption and anti-bribery activities and environmental protection.

The screening results serve as the foundation for indirect engagement activities. Through screening and engagement service providers, the Pension Fund participates in engagement discussions concerning the most serious norm violations. Several dozen engagement discussions take place each year, with other investors taking part as well. The impact of the dialogue is enhanced as the number of investors and share of ownership increase. For an investor with limited resources, the use of external engagement services is a cost-efficient means of implementing engagement dialogues with international companies.

The dialogue with companies is conducted through letters, teleconferencing and face-to-face meetings. In the planning phase of the engagement dialogue, the screening and engagement service provider drafts a list of measures which the company shall complete in order to remedy the shortcomings in their operations and to avoid new problems. The realised measures serve as signs of progress for the purpose of the engagement discussions. The company is removed from the monitoring list and the engagement dialogue ends once all measures have been completed.

Engagement activities require consistency and patience. All cases are different, and the achievement of positive results can take years. Occasionally, engagement efforts fail to change the company's operations and, in these cases, there shall be a consideration as to whether the investment should be divested from entirely. The Church Pension Fund invests in international markets via mutual funds, so it is not always possible to divest from individual holdings. For this reason, the screening results and their processing are a permanent part of the asset manager meetings.

Theme-specific proactive engagement. The Pension Fund participates in proactive engagement activities intended to influence companies in a constructive manner while taking into account the responsibility challenges of the future and the UN'S Sustainable Development Goals. The engagement activities are carried out in collaboration with an external expert. The engagement activities are targeted to specifically selected responsibility themes according to which the Fund strives to develop the operational methods of companies.

Such themes include, for example, the carbon risk to companies, fiscal responsibilities and the availability of clean water. An individual engagement project generally lasts approximately 2-3 years. Several institutional investors participate in each theme-specific engagement project.

Participation in investor initiatives. In an investor initiative, a group of investors combines its resources in order to present a joint message to a company. Normally, one owner or a group of owners acts as the founder and executor of the initiative. A large number of owners can participate in an investor initiative, and its intent is to get as broad and influential an ownership pool as possible to convince company management to change some aspect of the company's operations.

Through the international investor initiatives, the Pension Fund is involved in, for example, the development of corporate reporting practices. Among the key challenges for responsible investors is obtaining reliable and comparative information concerning the sustainable activities of companies. Since 2007, the Pension Fund has supported the CDP and its initiatives, such as *CDP Water Disclosure* and *CDP Carbon Action*. Through the CDP, the Pension Fund is involved in developing the climate change work and reporting of companies. These initiatives aim to ensure quality corporate responsibility reporting and to establish corporate objectives related thereto. The purpose of the initiatives is also to advise companies in the sustainable use of natural resources and energy, and to provide information about the climate impacts of greenhouse gas emissions.

With the publication of its Climate Change Strategy, the Pension Fund has committed to the use of different climate change tools, such as carbon footprint reporting and engagement. As a signatory of the *Montréal Carbon Pledge* initiative, the Pension Fund has committed to reporting on the carbon footprint of its investments each year. The Pension Fund also participates in the *Climate Action 100+* initiative, the aim of which is to influence the companies among the world's 100 highest greenhouse gas emitters. The aim is to curb the emissions of these companies and to strengthen the financial reporting and administration as related to the companies' climate risks.

The themes, duration and resource requirements for investor initiatives vary greatly. Some initiatives deal with corporate responsibility on a general level, such as compliance with international agreements and norms. Initiatives can also focus on a select corporate grouping, an individual company case or a theme, as a means of shifting the company's current method of operations into a more responsible direction. Participation is generally free, but it does require a certain amount of work input from the investor. The results of investor initiatives can be measured, for example, by looking at the target companies' response rate or by assessing the measure performed by the companies based on various recommendations.

The Pension Fund's objective is to participate in 2-4 initiatives each year as suits its available resources.

5.3 Impact investing

Impact investing refers to investments in companies, organisations or funds, whose purpose is to make investment returns along with a significant social or environmental impact. As regards the Church Pension Fund, the forms of investment that are considered impact investing include, for example, different micro loans and green bonds. The Pension Fund actively monitors impact investing and the development of its different forms.

6 Selection and monitoring of asset managers

The selection of asset managers is a critical phase in terms of responsible investment activities. ESG issues and related requirements should be thoroughly assessed when selecting a cooperative partner.

The Pension Fund encloses its guidelines for responsible investing in all requests for tenders, so that asset managers participating in the bidding are aware of the Pension Fund's expectations in relation to the offered investment strategy. The Pension Fund strives to assess the asset manager's responsible investment philosophy and whether or not the product being offered can be approved as part of the Pension Fund's investment portfolio.

Asset managers do not need to have all the processes related to responsible investing in use at the start of the co-operation, but rather, the Pension Fund can also work on initiating such practices together with the asset manager. The asset manager's commitment to the PRI provides a good foundation.

The Pension Fund assesses and monitors the following aspects of the asset manager's responsible investing capacity:



1. ESG profile of asset manager

A responsible investor also manages its own corporate responsibility issues well. The Pension Fund requires its asset managers to have responsible environmental and personnel policies, as well as an effective corporate governance approach.

2. Principles and internal processes

The Pension Fund determines how responsible investment fits into the asset manager's investment philosophy. Publicly available responsible investment guidelines and an ownership policy are the first demonstration that the asset manager is committed to such activities and their development. The Pension Fund is also interested in knowing how compliance with the guidelines is monitored within the organisation and who undertakes to ensure their implementation.

A committed asset manager communicates its responsible investment approaches to its personnel, customers, co-operative partners and other stakeholders. Active asset managers also participate, to the

extent allowed by their resources, in different responsible investing initiatives or forums that facilitate networking and inspire new investment ideas.

3. Resources and know-how

The Pension Fund is particularly interested in how the division of tasks within the investment team works in relation to the ESG analysis, what the team's level of expertise is and in what manner this expertise is further developed. Many asset managers use external ESG service providers, and the Pension Fund examines how the ESG information is used as part of the investment activities. The aim of the Pension Fund is to ensure that all ESG issues serve as the foundation for all investment analyses, not simply as a separate assessment phase. The portfolio managers and analysts should have their own views about the essential responsibility issues for different sectors and companies - and the asset manager should encourage its personnel to integrate the ESG issues into their investment analyses.

4. ESG integration

The Pension Fund wants to know which ESG issues are relevant to the asset manager's investment analysis. The next step is to clarify the way in which the ESG issues are involved in the investment decision-making process, and how this affects the asset manager's investment performance. One method to determine this is to ask the asset manager for concrete examples of how the ESG issues have impacted on individual investment decisions, both in terms of specific companies and sectors.

5. Active ownership and engagement

The Pension Fund wants to understand the content and practical realisation of the asset manager's ownership policy. The Pension Fund determines, by requesting detailed examples of realised ESG dialogues and other engagement processes, how the asset manager combines its engagement activities with its investment decision-making process. The Pension Fund favours asset managers that take advantage of their shareholder rights and consistently discuss ESG issues in corporate meetings and events. Active ownership practices, such as participation in annual general meetings, are very labour-intensive activities, and the Pension Fund recognises that it may not be possible for all asset managers to commit themselves to such practices. Furthermore, it should be noted that the active ownership practices to be used are specific to certain asset categories.

6. Reporting and communications

The Pension Fund clarifies the manner and frequency in which the asset manager provides reports on its responsible investment activities and results. The Pension Fund also monitors the reporting of the asset managers on the realisation of the UN's Sustainable Development Goals and emphasises the measurement of the ESG impacts of the investment activities. As a signatory of the Montréal Carbon Pledge initiative, the Pension Fund requires carbon footprint reporting on all its equity and corporate bond investments.

The Pension Fund opens up the content of its equity and fixed-income investments biannually for responsibility screening. Hence, the holdings of the mutual funds should be available when necessary. The Pension Fund also expects active communication from all the asset managers if, for example, it is discovered that the investment portfolio contains investment objects that operate in conflict with the investment principles of the Pension Fund.

The Pension Fund monitors the development of the responsible investment activities of its investment funds, in all asset classes, with the help of an annual ESG survey. The Pension Fund shares the survey results with its asset managers and discusses the development targets related to their responsible investment activities, if necessary.

7 Responsible investing in practice

The Church Pension Fund takes ESG issues into consideration in all asset categories. Every asset category involves different methods and possibilities to include ESG issues as part of the investment process.

Matters of responsibility are taken into account in the work of the Pension Fund's Investment Unit as part of the investment decisions made prior to actual investments. Often, the ideal moment to influence the operational principles of an asset manager and the investment fund in question is during the investment phase and related negotiations.

After the investment phase, the Pension Fund endeavours to continuously advance the asset manager's knowledge and skills by inquiring about and discussing their practices related to responsibility at collaborative meetings. The Pension Fund's annual ESG survey acts as a monitoring tool and concerns investments in all asset classes.

The Pension Fund primarily invests in funds registered in a state that is committed to the OECD's Automatic Exchange of Information (AEOI) agreement regarding tax matters.

If the asset manager or investment fund does not meet the responsibility demands set by the Pension Fund or there are open issues regarding their responsibility efforts, the Investment Unit will initiate an engagement dialogue with the asset manager.

7.1 Equity investments

The listed equity portfolio of the Pension Fund contains both direct equity investments and mutual fund investments.

Direct equity investments. The Church Pension Fund owns direct Finnish and European equities through three discretionary asset management agreements. A discretionary asset management agreement means that the Church Pension Fund is listed as an owner in the shareholder register, but a mandate manager is authorised to make the investment decisions on behalf of the Pension Fund. The agreement specifies the limitations of the investment activities, including the ESG criteria, and the asset manager must manage the Pension Fund's investments in accordance with the agreement. According to the agreement, the asset manager undertakes to consider ESG issues in its investment decisions, to serve as active owners and to report on its activities.

The Pension Fund participates in the annual general meetings of domestic listed companies in co-operation with its asset managers.

Indirect equity investments. In addition to discretionary asset management agreements, the Pension Fund has mutual funds for equity investments in different geographical areas. The Pension Fund selects asset managers that have proven their commitment to responsible investing by signing the Principles for Responsible Investment (PRI) and by drafting their own responsible investment rules. Such asset managers consistently incorporate ESG issues into their investment analyses through different methods, take advantage of their shareholder rights at annual general meetings and discuss responsible practices with companies.

The Pension Fund carries out a biannual, norm-based responsibility screening of all its equity investments and participates in engagement activities.

Equity index investments. In order to achieve a tactical allocation, the Pension Fund uses so-called passive investment methods such as equity index funds. Equity index funds offer the Pension Fund a liquid and cost-efficient means of participating in different equity markets. They facilitate the smooth change in allocation between the different market areas within the stock portfolio. The purpose of index funds is to acquire market-specific emphasis, not to focus on individual companies.

The asset manager that administers the Pension Fund's equity index funds complies with a broad set of responsibility criteria. All of the index funds use responsibility screening; no investments are made in companies that violate international norms concerning human rights, labour law, corruption and the environment. Additionally, investments are not made in companies that are involved in coal mining operations or coal burning. Any affiliation with the manufacturing of key components for controversial weapons will also lead to a company being excluded. Furthermore, all index funds actively use the right to vote in annual general meetings worldwide.

7.2 Fixed-income investments

The fixed-income investments of the Pension Fund are generally managed through mutual funds.

Government bonds. Government bond investments finance state activities. The Pension Fund favours asset managers that evaluate ESG issues in target states. This is particularly crucial for asset managers investing in government bonds offered by developing countries. In such cases, the asset managers should consider the degree to which the countries in question comply with international agreements and recommendations relating to human rights, the environment and other sustainable development issues.

Corporate and convertible bonds. The Pension Fund selects asset managers that have proven their commitment to responsible investing by signing the Principles for Responsible Investment and by drafting its own responsible investment rules. Such asset managers consistently incorporate ESG issues into their investment analyses through different methods and discuss responsible practices with companies.

Money-market investments. The Pension Fund requires that the depository bank acts responsibly and that the managers of the money-market funds consider ESG views in as far as the issuers are concerned.

The Pension Fund carries out a biannual, norm-based responsibility screening of all its government bond, corporate bond and money-market investments and participates in engagement activities.

7.3 Alternative investments

The Pension Fund's alternative investments include real estate, private equity, alternative fixed-income and absolute return investments.

Real estate investments. The Church Pension Fund is a long-term real estate investor that complies with the principles for responsible investing and requires responsible and socially acceptable practices from its co-operative partners as well.

Responsible real estate investing places an emphasis on environmental issues. This is due to the fact that since property and construction play a significant role in the consumption of energy and natural resources,

the creation of emissions and, thereby, have an impact on climate change. The construction sector also has a positive impact on employment, and the condition of the properties has a direct influence on the lessees and the attraction of the surrounding areas. The Church Pension Fund considers ESG issues in both direct real estate investments and property fund investments.

In direct real estate investments, the Pension Fund considers the responsibility angle by, among other actions, maintaining the condition of its real estate properties and developing them in an environmentally-responsible manner. Energy efficiency, sustainable development and ecological aspects, in particular, are taken into consideration on the properties. Additionally, special attention is paid to responsibility throughout the building life cycle and to the overseeing of labour obligations and occupational safety and health issues concerning subcontractors. Energy issues are taken into consideration, especially when any basic repairs are done to the properties. Sustainable development solutions play a central role in the acquisition of new properties.

Responsible real estate investing involves a great deal of interaction: co-operative companies are encouraged to act responsibly and efforts are made to motivate the managing directors of the real estate companies to incorporate responsibility into the management of properties. The Pension Fund works together with lessees to find the best practices, for example, when negotiating on new rental agreements.

Within its *property fund investments*, the Pension Fund carries out its own ESG evaluation as part of the investment assessment of new property funds. The responsibility level of property funds is assured through the use of side letters that are appended to the fund agreement. In the ESG side letter, the fund management company commits to take ESG criteria into consideration in its investment decisions and to strive to integrate the criteria into its investment selection and reporting. In terms of property funds, the focus may be on energy-efficiency, the use of renewable energy, public transportation solutions and the certification of properties.

Private equity investments. Private equity is interesting from a responsible investment perspective: the private equity investor, as the owner, has the opportunity to influence company operations at an early phase, thereby helping to construct a sustainable corporate culture. The private equity investor can also support new domestic innovations and entrepreneurship, and invest in renewable energies and clean technologies.

The private equity investments of the Church Pension Fund consist of private equity funds, which have many other investors. Some of the funds are so-called fund of funds, which invest in other private equity funds.

The Church Pension Fund has outsourced the monitoring and administration of its private equity fund investments to an external co-operative partner. The co-operative partner conducts an ESG evaluation of new private equity funds as part of a more comprehensive investment assessment. The responsibility of a private equity fund is assured through the use of side letters that are appended to the fund agreement. In the side letters, the management company undertakes to take responsibility criteria into account in its own investment activities. As part of its ongoing monitoring, the Pension Fund's co-operative partner conducts an annual ESG survey for all private equity funds.

The Pension Fund requires that the fund management companies for private equity funds meet their tax obligations in the manner intended by the valid laws and decrees, both in terms of their own activities as well as that of the portfolio companies within their authority. The Pension Fund views it as important that the fund management companies and portfolio companies pay their taxes to the administrative district in which they operate and in which the revenue-generating financial activities or work are understood to take place.

Alternative fixed-income investments. Alternative fixed-income investments are alternative funding channels offered alongside traditional bank loan funding. Alternative fixed-income investments include, for example, private credit and microcredit funds. The Pension Fund only invests in funds that have a good reputation and act in a responsible manner. As part of its fund selection process, the Pension Fund requires potential investment objects to commit to the ESG principles, to integrate responsibility issues into investment decisions and to provide regular reporting to investors.

Absolute return investments. The Pension Fund only invests in funds that have a good reputation and act in a responsible manner. As part of its fund selection process, the Pension Fund requires its investment objects to commit to the ESG principles, to integrate responsibility issues into investment decisions and to provide regular reporting to investors.

8 Reporting

The Church Pension Fund describes the results of and actions related to its responsible investment activities in its *annual report*. The annual report covers the following activities:

- Monitoring and annual comparison of tools related to the climate change strategy
- Carbon footprint of equity and corporate bond investments
- Results of the ESG survey targeted at asset managers
- Responsibility screening of the portfolio and related engagement discussions
- Participation in annual general meetings
- Investor initiatives and their progress.

Another important reporting tool is the *annual report drafted for PRI*, which details the realisation of the PRI principles within the Pension Fund’s activities. The Pension Fund’s annual reports on PRI and responsible investments are public reports.

The Pension Fund wants to evaluate the possibilities to integrate ESG ratings and impact indicators into the monthly and annual reporting. The *UN’s Sustainable Development Goals* provide a key framework for impact reporting.

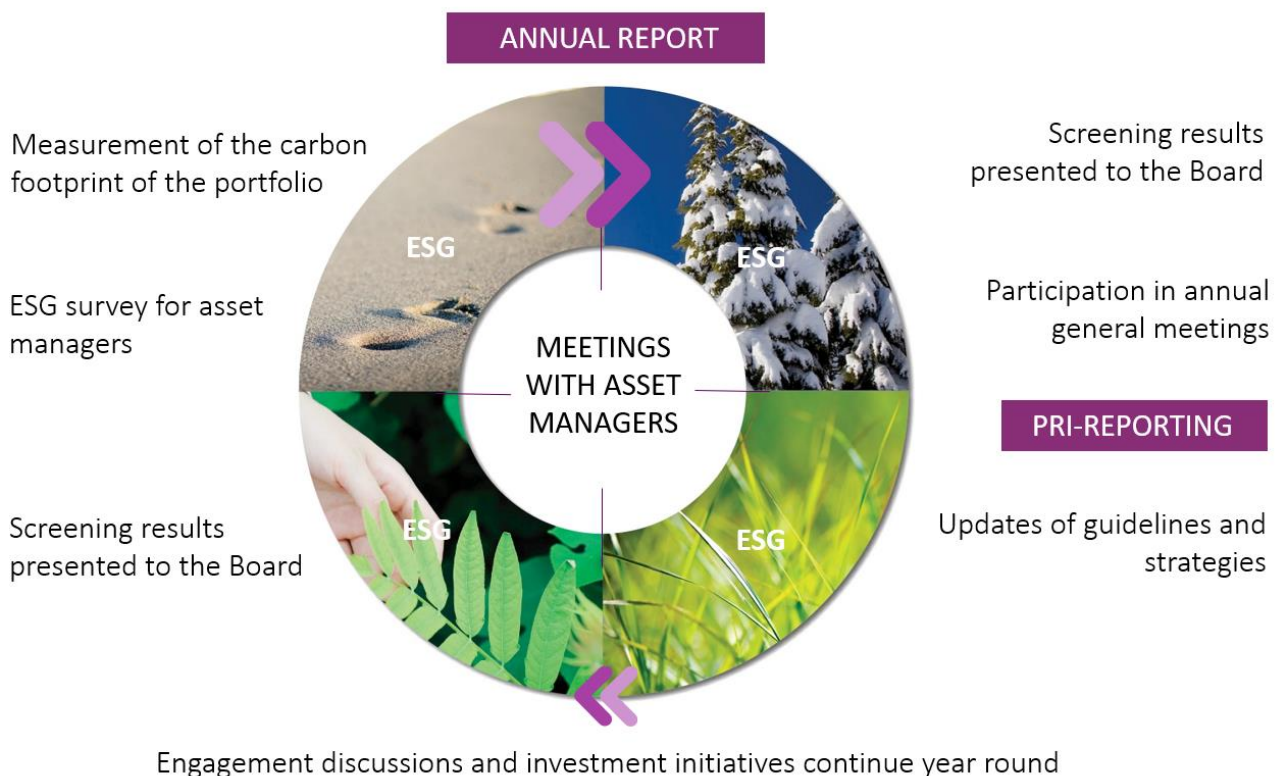


Figure: Annual schedule for the responsible investment activities and related reporting of the Pension Fund

9 Decision-making process

The responsible investment activities of the Church Pension Fund are prepared and executed in four different stages:

- The **Board of the Pension Fund** approves the responsible investment guidelines, the Climate Change Strategy and the annual reports. Support for the responsible investment activities is included in the Board's tasks, and all related activities are discussed regularly in the meetings of the Board.
- The **Responsible Investment Work Group** is an expert body that advises the Board of the Pension Fund on responsible investing and in matters related to corporate responsibility. The Work Group prepares the responsible investment guidelines and the Climate Change Strategy, and makes recommendations to the Board with regard to issues related to responsible investing.
- The **Director of the Church Pension Fund** approves participation in international investor initiatives and the decision is reported to the Board.
- The **Pension Fund's Investment Unit** is responsible for all investment activities and related reporting. The Investment Unit handles, on a case-by-case basis, any news that arises regarding the responsible practices of companies and communicates with the different relevant stakeholders.

THE CHURCH PENSION FUND 

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