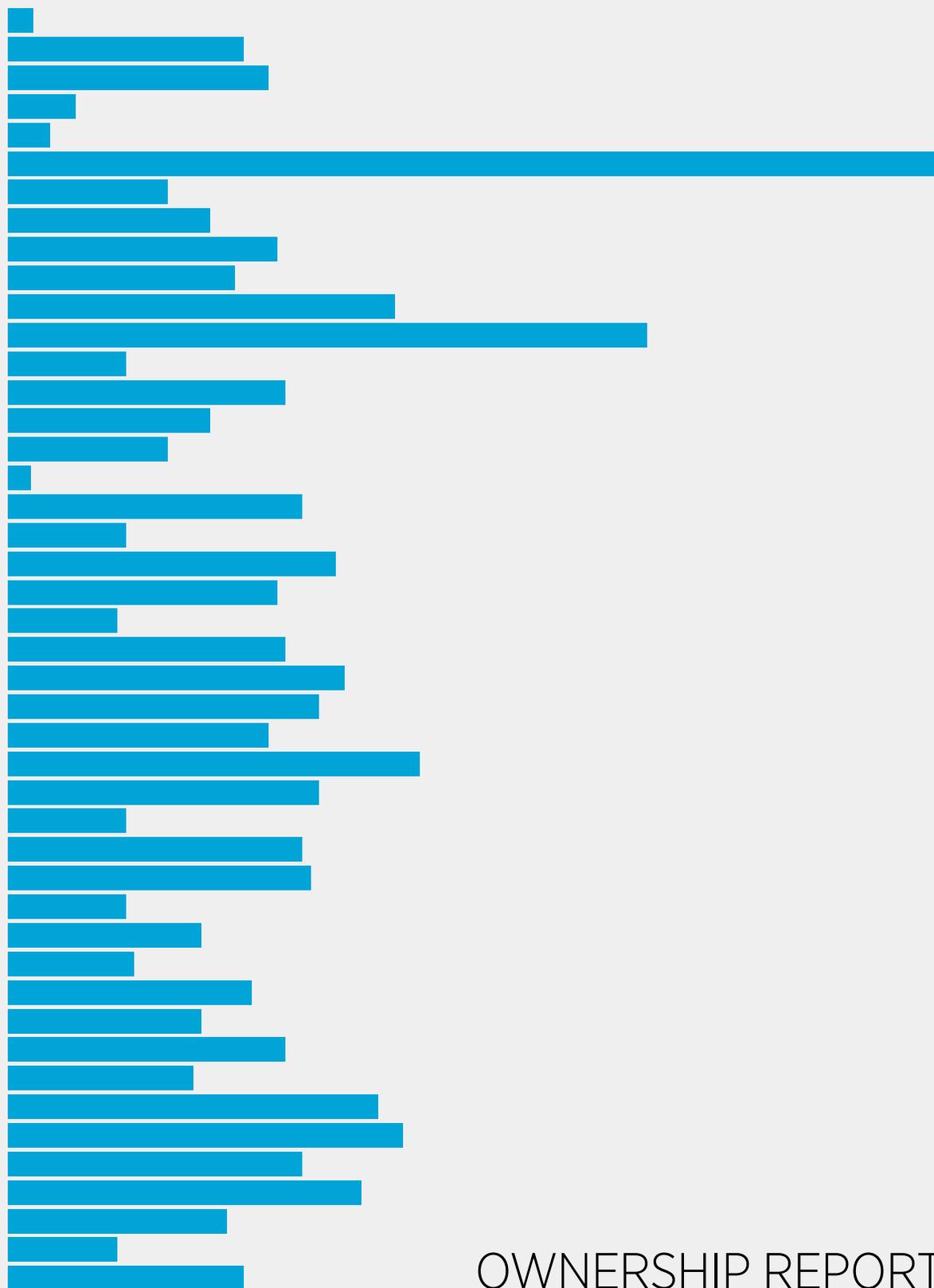


# Folketrygdfondet





<b>4</b>	<b>INTRODUCTION</b>
4	In brief
6	Managing director's comments
8	What, where and how?
<b>10</b>	<b>RESPONSIBLE INVESTMENT</b>
10	Our priorities: reducing risk and creating value
11	The importance of a Nordic presence
12	Key ownership issues
<b>13</b>	<b>ACTIVE EQUITY OWNERSHIP IN THE PAST YEAR</b>
13	Dialogue
14	Dialogues with portfolio companies
15	Shareholders' meetings, Norway
19	Focus topic: the increasing importance of proxy agents
20	Shareholders' meetings, Nordic region
22	Nomination committees and governing bodies
24	ESG analyses and focus areas
27	Focus topic: CO <sub>2</sub> analysis of the portfolio
<b>28</b>	<b>EXERCISE OF CREDITOR RIGHTS IN THE PAST YEAR</b>
28	The fixed-income portfolio: closer follow-up of issuers
<b>30</b>	<b>TOOLS AND INITIATIVES</b>
30	Guiding documents
31	External initiatives
<b>32</b>	<b>MANDATES, GUIDELINES AND PRINCIPLES</b>

# MANAGING PUBLIC FUNDS

## THE GOVERNMENT PENSION FUND

... shall support government saving to finance the National Insurance Scheme's expenditure on pensions and support long-term considerations in the use of petroleum revenues...

**From the Government Pension Fund Act**

### THE GOVERNMENT PENSION FUND GLOBAL

is managed by Norges Bank

NOK  
**4.397**  
billion as per the second quarter

Receives new funds from the petroleum industry. Helps to cover expenditure in the government budget. See also the "fiscal rule".

### THE GOVERNMENT PENSION FUND NORWAY

is managed by Folketrygdfondet

NOK  
**151**  
billion as per the second quarter

Norwegian equity portfolio	<b>50.2%</b>
Norwegian fixed-income portfolio	<b>34.5%</b>
Nordic equity portfolio	<b>8.9%</b>
Nordic fixed-income portfolio	<b>6.4%</b>

"Closed fund": does not receive new funds, and returns are accumulated. The original capital derives from national insurance scheme surpluses in the period 1967-1979.

### THE GOVERNMENT BOND FUND

is managed by Folketrygdfondet

As per the second quarter, the invested share of the Government Bond Fund totalled NOK 3.1 billion. The Fund is not part of the Government Pension Fund, and was introduced as a measure during the 2009 financial crisis.

**Folketrygdfondet is a company by special law** which manages the Government Pension Fund Norway according to a mandate given by the Ministry of Finance. Folketrygdfondet also manages the Government Bond Fund. The capital is deposited as contributions in Folketrygdfondet and is invested in Folketrygdfondet's name.

## RETURN OVER TIME

The objective for the management of the Government Pension Fund Norway is to achieve the highest possible return over time, within certain limits.

The average annual return has been 6.0 per cent over the last five years – 1.0 percentage point above the benchmark indices used to evaluate the management of Folketrygdfondet. See the Q2 2013 report on [www.ftf.no](http://www.ftf.no).

For Folketrygdfondet, responsible investment is about reducing risk and achieving a return over time. We have financial reasons for evaluating portfolio companies' actions in relation to environmental, social and corporate governance issues (ESG issues). As a large, long-term investor, we also have a financial motivation to invest in measures to ensure well-functioning capital markets in Norway and the Nordic region.

Our mandate is based on the conviction that a solid return over time is dependent on sustainable development in an economic, environmental and social sense. Folketrygdfondet will follow recognised principles for responsible investment and active ownership, and will contribute actively in the development of good national standards.

### **Importance for the business sector**

This mandate gives Folketrygdfondet an important role beyond that of achieving a solid financial return for the public purse.

Folketrygdfondet supports business-sector development:

- with capital
- through good active ownership
- by promoting more stable, well-functioning markets.

### **The active ownership framework**

Folketrygdfondet conducts company follow-up through dialogue with senior executives and boards of directors, voting at shareholders' meetings and participation in nomination committees, corporate assemblies and shareholders' committees.

Folketrygdfondet may not sit on the boards of portfolio companies, and may only own up to 15% of the shares issued by Norwegian companies and up to 5% of the shares in companies listed on other Nordic stock exchanges.

### **Reporting**

Our mandate states that Folketrygdfondet must report annually on its exercise of active ownership and how good corporate governance and environmental and social considerations are integrated into management activities. We have chosen to do this in the form of a dedicated ownership report that is published after the shareholder meeting season.

MANAGING DIRECTOR OLAUG SVARVA

## OUR VISION: TO IMPROVE THE MARKETS IN WHICH WE OPERATE

At Folketrygdfondet, we want to support the healthy, profitable development of the companies in which we invest and the markets in which we operate. We aim to promote proper conduct and a clear division of roles, and our reason for doing so is always financial.

**Folketrygdfondet is the** largest institutional investor on the Oslo Stock Exchange. As per the end of the second quarter, Folketrygdfondet's investments accounted for 10 percent of the main index and 5 percent of total assets. Our task, on behalf of the public, is to manage these funds with a long-term perspective, and to achieve the best possible return within defined risk limits.

We deal extensively with the Norwegian business sector, and have long-standing relationships with Norwegian companies.

### Our reason for doing so is always financial

Although we are a smaller stakeholder, relatively speaking, in the other Nordic markets, and therefore play a different role, our investment activities and active ownership in Danish, Finnish and Swedish companies are guided by the same principles as in Norway.

Good corporate governance is about protecting the rights of owners and other stakeholders in companies and ensuring that good corporate governance structures are in place. The overarching objective of all corporate governance is to ensure the best possible value creation over time.

Folketrygdfondet aims to be a strong representative for minority shareholders in the Norwegian market, and a guiding principle in this context is the equal treatment of all shareholders. This objective has played a central role since the early 1990s, when Folketrygdfondet was first permitted to invest in shares. In specific individual cases, we, along with other minority shareholders, have a clear interest in ensuring that the rules are followed and that the interests of all shareholders are protected. Over time, however, this also involves

The general practice related to corporate governance in the Norwegian business sector has improved. Folketrygdfondet plays a role in this, which we take seriously

preserving general confidence in the Norwegian stock market.

As described in this report, Folketrygdfondet attends the shareholders' meetings of its portfolio companies. As many shareholders do not vote at shareholders' meetings, Folketrygdfondet's share of the vote and influence are higher than our actual shareholding would suggest.

However, as we also show in this report, our relatively high share of the vote does not necessarily mean majority support and success in the short term. This year we again voted against the executive remuneration statements of several companies because they did not comply with our guidelines. Nevertheless, I would like to highlight executive remuneration schemes in particular as an example of longer-term success in implementing the attitudes and principles we share with other central stakeholders: none of the large, established companies on the Oslo Stock Exchange remain on the list of companies in which we vote against the executive remuneration statement.

Generally speaking, we can say that corporate governance practices in the Norwegian business sector have improved. Folketrygdfondet plays a role in this, which we take seriously. We also know that our efforts in this area must continue.

Folketrygdfondet is a performance-oriented investment institution. Our focus is on return, risk, commercial opportunities and competitive advantages. That is why we also search systematically for information on the portfolio companies. Our

reason for doing so is always financial.

We know that our questions about corporate governance, environmental challenges and social matters may sometimes be interpreted as attempts to act in a “politically correct” manner. That is not the point. The markets value information, and investors also demand information on environmental and social matters. This is an important trend, and we are seeing the increasing adoption of statutory reporting requirements both nationally and internationally.

### « A long-term investor cannot ignore the threat of climate change

We support this development, for one simple reason: companies that are good at providing the market with relevant information will win trust, reduce uncertainty about their operations and enable investors and other interested parties to assess the risk involved in investing. This will give the companies lower cost of capital than their competitors.

One area that is very much in focus at present, and which we expect to attract further attention in future, is climate change. Folketrygdfondet is a long-term investor, and therefore cannot ignore the threat of climate change. At the same time, we are a large investor on the Oslo Stock Exchange, where many companies operate in sectors with a large carbon footprint.

This year, we conducted our first analysis of greenhouse gas emissions from the companies in our portfolio to improve our understanding of the long-term risks in this area.

Some companies will be more vulnerable than others to potential direct and indirect costs in the form of higher CO<sub>2</sub> taxes, new regulations and customer demands. The long-term profitability of



our portfolio may be affected by how companies handle their greenhouse gas emissions, and this is therefore an issue we raise with them. It is the companies' boards of directors that must adopt strategies for dealing with greenhouse gas emissions. They should take a proactive approach to risks and opportunities, and in our role as investor we expect information on their efforts in this area.

Our aim is to be an engaged but predictable owner. In this annual ownership report, the seventh we have published, we discuss our ownership principles and their practical implementation. It is important that companies, other shareholders and everyone else who is interested in our activities can familiarise themselves with the principles we follow, and can check that we act as we have said we will.

## WHAT, WHERE AND HOW?

Folketrygdfondet's responsible investment principles are the same for the entire portfolio, but our approach is adapted for the different sub-portfolios. This is how we exercise our ownership:



**NORWEGIAN EQUITY PORTFOLIO**      MV (NOK million): 75,805      Number of companies: 47

**Ten largest investments**      **NOK million**

Statoil	13,448
Telenor	9,435
DNB	8,703
Yara International	4,418
Seadrill	4,068
Orkla	3,722
Subsea 7	3,294
Schibsted	2,397
Marine Harvest	2,112
Norsk Hydro	2,012

- **DIALOGUE:** Ongoing dialogue with portfolio companies and additional dialogue as needed. See page 13.
- **SHAREHOLDERS' MEETINGS:** Participate in all, directly or by proxy. See page 15.
- **ESG:** Analyses of all companies. In addition, focus areas. See page 24.
- **NOMINATION COMMITTEES, ETC.:** Participate in and make suggestions to nomination committees and governing bodies. See page 22.
- **EXTERNAL INITIATIVES:** Participate in initiatives and cooperate with other investors. See page 31.

**NORDIC EQUITY PORTFOLIO**      MV (NOK million): 13,506      Number of companies: 97

**Ten largest investments**      **NOK million**

Novo Nordisk	1,520
Nordea Bank	786
Ericsson	763
Hennes & Mauritz	724
Volvo	666
Atlas Copco	546
Danske Bank	383
Sampo	379
SCA	372
Investor	369

- **DIALOGUE:** Monitoring of portfolio companies and additional dialogue as needed. See page 13.
- **SHAREHOLDERS' MEETINGS:** Access to analyses. Vote at all by proxy. See page 20.
- **PARTICULAR TO THE NORDIC PORTFOLIO:** Implement exclusion decisions made by the Ministry of Finance on the recommendation of the Council on Ethics. See page 11.

**NORWEGIAN FIXED-INCOME PORTFOLIO**      MV (NOK million): 52,138      Number of bond loan issuers: 159

**Ten largest investments**      **NOK million**

The Norwegian State	10,477
DNB Boligkreditt	4,181
Sparebank 1 Boligkreditt	2,587
Nordea Eiendoms-kreditt	2,301
Statoil	2,086
DNB Bank	1,512
Eika Boligkreditt	1,262
Bergenshalvøens Kommunale Kraftselskap	1,094
Eksporthfinans	968
Kommunal Landspensjonskasse	952

- **DIALOGUE:** Monitoring of portfolio companies and additional dialogue as needed.
- **DEFAULT SITUATIONS:** Participate in bondholders' meetings. Active involvement in restructuring.
- **ESG:** Taken into account in credit risk assessment.
- **REQUIREMENT FOR FIXED-INCOME INVESTMENTS:** Invest only in loans with an appointed trustee. See pages 13 and 28.

**NORDIC FIXED-INCOME PORTFOLIO**      MV (NOK million): 9,603      Number of bond loan issuers: 46

**Ten largest investments**      **NOK million**

The Republic of Finland	1 366
The Kingdom of Denmark	1,138
Stadshypotek	865
The Kingdom of Sweden	775
Swedbank Hypotek	731
Danske Bank	460
Nordea Kredit Realkreditaktieselskab	351
Skandiviska Enskilda Banken	348
Nordea Bank	333
Svenska Handelsbanken	282

- **DIALOGUE:** Monitoring of portfolio companies and additional dialogue as needed. See page 13.
- **DEFAULT SITUATIONS:** Owns smaller stakes, therefore a less active role in this context.
- **PARTICULAR TO THE NORDIC PORTFOLIO:** Implement exclusion decisions made by the Ministry of Finance on the recommendation of the Council on Ethics. See page 11.

## OUR PRIORITIES:

## REDUCING RISK AND CREATING VALUE

Folketrygdfondet exercises its role as owner in many arenas – in direct contact with senior company executives and boards of directors, in shareholders' meetings, in corporate assemblies or shareholders' committees, and in nomination committees.

**Over time, dialogue** with portfolio companies has become our most important ownership tool. Such direct contact enables us to understand strategies, challenges and risks.

Our ownership stake in companies listed on the Oslo Stock Exchange may not exceed 15 percent, and we are not permitted to sit on the boards of portfolio companies. The purpose of these rules is to protect Folketrygdfondet's role as a financial investor.

**Engaged but predictable**

We aim to be an engaged but predictable owner with a transparent and familiar way of working.

To understand Folketrygdfondet's active ownership, it is important to consider the division of ownership on the Oslo Stock Exchange. There are currently three main categories of owners: the public sector, which owns 35.5 percent of total assets, foreign investors, who together own 36.4 percent of total assets but exercise varying degrees of active ownership, and privately owned Norwegian companies, who account for 14.5 percent of total assets and often have one dominant, active owner.

Folketrygdfondet is the largest financial investor in this investor landscape, holding 5 percent of the assets listed on the Oslo Stock Exchange. We exercise ownership in companies with very different ownership constellations. Although we always apply the same principles, in practice the best exercise of our role will have to vary according to the ownership structure of each individual company.

**Looking to invest in high-quality companies**

Our objective is to have access to the best possible information when making investment decisions, and this motivates us to conduct quantitative and qualitative analysis of companies. We are focused on return, risk, commercial opportunities and competitive advantages.

Folketrygdfondet's size in the Norwegian market

means that we are less able than many other investors to swiftly enter and exit individual companies. Our ownership stakes in the Norwegian market are relatively large, and once we have chosen to invest in a company we will generally hold on to the investment for a number of years.

The search for high-quality investment targets is therefore a major priority for Folketrygdfondet.

Our portfolio managers apply a set of evaluation criteria covering not only companies' handling of key ownership issues, but also macroeconomic assessments and quantitative evaluations of factors such as performance development, return on net capital, capital structure, pricing and cash flow. Sometimes, qualitative considerations will weigh so heavily that we decide not to invest in a company even though the investment could have generated a strong financial return in the short term.

**The trend we see**

The portfolio companies are subject to various reporting requirements that are important for our risk assessments, valuations and investment decisions. In many cases, statutory reporting requirements are based on recommendations and standards that the companies have already adopted. We see a trend towards making reporting requirements statutory, but leaving the scope and degree of detail to be determined by each individual company. If the resulting reports are to be of value, the information that is provided must be specific and relevant, and must relate to the most important risk factors to which the company is exposed.

Not all companies can turn environmental considerations or other social matters to their competitive advantage. However, every company can reduce uncertainty about its own operations. We expect boards of directors to deal with this issue effectively by being open about and relating the dilemmas they face.

## THE IMPORTANCE OF A NORDIC PRESENCE

We are concerned with the same ownership issues throughout the portfolio, and apply the same principles and guidelines in respect of the Nordic and Norwegian portfolios. However, our relative size is smaller in the Nordic markets.

**At any given time**, approximately 15 percent of the portfolio of the Government Pension Fund Norway is invested in shares and bonds issued by companies listed on regulated exchanges in Denmark, Finland and Sweden. Folketrygdfondet may own up to 5 percent of any individual company listed on such Nordic exchanges.

Because Folketrygdfondet's ownership stakes are smaller and spread among more companies, our active ownership is less intense in the Nordic portfolio than in the Norwegian portfolio.

### Building up our knowledge base

In the management of our Nordic investments, we cover all sectors and, in particular, companies operating in areas in which we have specialised knowledge. The interplay between our Norwegian and Nordic portfolios increases our knowledge and skill as an investor. Our position as a relatively small stakeholder in the Nordic region as a whole gives us greater flexibility to make changes to the portfolio.

Holding active positions in the Nordic region gi-

ves us broader insight into macroeconomic trends, improves our sector knowledge and provides us with a better basis for evaluating market prices, including of Norwegian shares. Moreover, our Nordic investments show us how ownership issues are dealt with and developed in other markets. In our experience, our presence in Denmark, Finland and Sweden has strengthened our investment expertise and the results we achieve.

### Exclusion of companies

An important difference between our investment activities in Norway and the rest of the Nordic region is that the Nordic portfolio is subject to the Ministry of Finance's decisions regarding the exclusion of companies from the investment universe of the Government Pension Fund Global. Such decisions are made by the Ministry on the recommendation of the Council on Ethics.

➤ See [www.finansdepartementet.no](http://www.finansdepartementet.no)

### INSTRUMENTS USED IN OUR RESPONSIBLE INVESTMENT ACTIVITIES

Portfolio	ESG considerations* in management	Exclusion	Dialogue with portfolio companies	Voting at share- holders meetings
Norwegian shares	■	—	■	■
Nordic shares	■	■	■	■
Norwegian bonds (corporate)	■	—	■	N/A
Nordic bonds (corporate)	■	■	■	N/A
Government bonds	—	—	N/A	N/A

\* "ESG considerations" means that we analyse and monitor how portfolio companies handle environmental, social and corporate governance issues.

## KEY OWNERSHIP ISSUES

Folketrygdfondet does not sit on the boards of portfolio companies, and we emphasise the importance of ensuring the clear definition of roles and allocation of responsibilities between company boards and shareholders. The shareholders' meeting is the supreme governing body of a company, and the most important arena for shareholders. The issues discussed below are ones we consider important to us, in which we get involved and on which we will have opinions at shareholders' meetings and in other relevant forums.

### CAPITAL STRUCTURE AND STRATEGY

We will have opinions on return targets, share issues, dividends and authorisations to issue shares. We will also have opinions on the consequences of company strategy for capital structures, returns and risk levels.



### REMUNERATION

We emphasise that portfolio companies must provide clear, reliable information on their executive remuneration schemes and the costs associated with them. In our view, schemes must be performance-related to ensure alignment between the interests of the shareholders and those of senior executives. The schemes must be reasonable in scope and not based on external circumstances outside the control of senior executives.



### BOARD COMPOSITION AND GOVERNING BODIES

We emphasise good processes for identifying qualified candidates and ensuring the right assortment of expertise. We also emphasise securing support from the largest shareholders.



### REPORTING AND COMMUNICATION

We expect portfolio companies to communicate financial information to the market and to explain values, governance principles, environmental and social matters in a relevant and correct manner.



### VALUES AND GOVERNANCE PRINCIPLES

We expect portfolio companies to develop governance principles, guidelines and procedures for relevant environmental and social matters, and to follow them in their operations.



## DIALOGUE:

## RAISING SPECIFIC CASES

In the past year, we have had meetings with 17 companies in Norway regarding key ownership issues and specific incidents. These meetings are in addition to our ongoing contact with portfolio companies in the course of day-to-day management.

**Being a large** shareholder confers obligations. We are available to the portfolio companies, and expect the companies to be available to us. In the Norwegian market, we have regular meetings and contact with senior company executives, including the board chair on matters falling within the board's area of responsibility. For Folketrygdfondet, ongoing dialogue with portfolio companies is a well-established means of monitoring its investments.

The instrument of dialogue suits Folketrygdfondet, and is vital for us because we are a large, long-term investor. Conversations with company executives give us a basis for understanding performance developments, strategy, the competitive situation, growth opportunities, environmental challenges and relevant social factors. This in turn makes us a better owner, not least because we can evaluate companies' capital needs and strategic changes quickly.

The table on the following page summarises the dialogues Folketrygdfondet has conducted with companies on key ownership issues and specific incidents. The table does not include conversations and meetings held with portfolio companies as part of Folketrygdfondet's day-to-day management.

### Agenda items at shareholders' meetings

If we can achieve movement in the right direction on a matter, we are more likely to choose compromise rather than confrontation. Over time, we have seen that this approach produces positive results.

Ahead of this year's shareholders' meetings in Norway, we raised matters such as:

- authorisations to issue shares
- executive remuneration
- board composition.

In some cases, our input was adopted, enabling us to vote for the board's executive remuneration statement at the shareholders' meeting. In other cases, we were

assured that our input would be adopted. Generally speaking, we have seen a clear improvement over time in how boards of directors handle share issues and executive remuneration schemes. See also page 15.

### The Nordic region

We continued to develop our active ownership activities in Sweden, Denmark and Finland in 2012. We concluded an agreement with an external service provider, effective as of 1 December 2012, for assistance in monitoring, analysing and conducting dialogue with portfolio companies when incidents requiring follow-up are discovered. During the first six months of the agreement, the external service provider conducted dialogue with nine companies. See the table on the following page.

### The fixed-income portfolio

We also concluded a monitoring agreement for the fixed-income portfolio last year, thereby securing a better basis for initiating dialogue with bond issuers when the need arises. See the separate article on follow-up of the fixed-income portfolio on page 28.

## OUR PROCEDURES FOR

### DIALOGUE

- We have meetings with the administration to monitor the company's development.
- We communicate with the board chair about matters falling within the board's area of responsibility.
- Folketrygdfondet and the portfolio companies are both aware that we should not receive inside information.
- Special procedures are followed if, in special cases, we do receive inside information.
- There must always be full transparency about the principles we apply and the methods we may use in our active ownership.
- In individual cases, however, transparency considerations must be balanced against considerations related to ongoing processes.

From Folketrygdfondets eierskapsutøvelse [Folketrygdfondet's active ownership], June 2012

## DIALOGUE WITH PORTFOLIO COMPANIES

The dialogues described in the tables below concern selected ownership issues. In some cases, we have contacted the company in question after an incident has occurred. In most cases, we have initiated discussions to survey risks and contribute to better follow-up of concrete cases and topics by the company. As regards capital structure and strategy issues, we have only included cases in the table that we have voted on at shareholders' meetings in our capacity as a shareholder. The table does not include conversations and meetings held with the portfolio companies as part of Folketrygdfondet's regular gathering of information about the companies' financial development. Nor does it detail our contact with nomination committees.

### NORWAY

Sector	Topic
Energy	<ul style="list-style-type: none"> <li>■ Executive remuneration</li> <li>■ The company's handling of and reporting on environmental, social and corporate governance issues (ESG issues), with a particular focus on anti-corruption activities and the environment</li> <li>■ Working conditions, workers' rights</li> <li>■ Reporting on greenhouse gas emissions</li> <li>■ Environmental risk associated with operations relating to the production of unconventional oil and gas resources</li> <li>■ Review of shareholders' meeting agenda items</li> <li>■ Establishment of corporate assemblies</li> </ul>
Health	<ul style="list-style-type: none"> <li>■ Executive remuneration</li> </ul>
Manufacturing industry	<ul style="list-style-type: none"> <li>■ Anti-corruption activities</li> <li>■ Reporting on greenhouse gas emissions (two companies)</li> <li>■ Sale of equipment for use in tobacco-sorting</li> <li>■ Environment: ballast water management, NOx and SOx emissions</li> <li>■ Positive feedback on guidelines, procedures and reporting related to environmental and social matters</li> </ul>
Consumer staples	<ul style="list-style-type: none"> <li>■ Sea lice, escape and other environmental issues (three companies)</li> <li>■ Acquisition of a company (two companies)</li> <li>■ Authorisations at shareholders' meetings</li> <li>■ Executive remuneration</li> </ul>
Materials	<ul style="list-style-type: none"> <li>■ Sustainability reporting</li> <li>■ Executive remuneration statement</li> </ul>
Telecoms	<ul style="list-style-type: none"> <li>■ Anti-corruption work</li> <li>■ Human rights</li> </ul>

### NORDIC REGION

Country	Sector	Topic
Denmark	Manufacturing industry	Human rights
	Manufacturing industry	Indigenous peoples' rights
	Materials	Environment
Finland	Information technology	Human rights
	Consumer goods/	Workers' rights
	Information technology	Human rights
Sweden	Consumer goods	Workers' rights, labour standards
	Finance	Workers' rights
	Telecoms	Corruption and human rights

## SHAREHOLDERS' MEETINGS, NORWAY:

# VOTED AGAINST FIVE EXECUTIVE REMUNERATION STATEMENTS

Folketrygdfondet voted against a total of 12 board proposals at five shareholders' meetings this year, including voting against the executive remuneration statements of all five companies involved.

**This year**, we again voted against the executive remuneration statements of Algeta, Atea and RCCL. We also voted against the executive remuneration statements of Spectrum and Lerøy for the first time.

Noreco, against whose executive remuneration statement we voted last year, was no longer part of the Folketrygdfondet portfolio as per the end of Q2 2013.

## Our reasons for voting against executive remuneration statements

Folketrygdfondet looks favourably on executive remuneration schemes that are goal-oriented and performance-related, and has clear expectations of companies' executive remuneration statements. They should be clear and explanatory, and must differentiate between executive remuneration policy and the schemes that are actually introduced. An executive remuneration statement should define both satisfactory goal achievement and the frameworks and ceilings applicable to share-based incentive schemes.

Where we have voted against an executive remuneration statement, we have done so because the company has not given a satisfactory account of its share-based incentive scheme, or because we consider the scheme too broad.

## Positive developments

From our perspective as a shareholder, we have observed positive developments in the Norwegian business sector with regard to options and executive remuneration schemes. Overall, fewer matters now require a response from us, and our general impression is that most companies are meeting our expectations relating to orderly executive remuneration schemes. None of the larger, well-established companies are found on the list of companies against whose executive remuneration schemes we

have voted in recent years.

Many of the companies in which this has been an issue have been young companies at special developmental stages.

## Satisfactory explanations

We see wide variations in the quality of executive remuneration statements. Kongsberg Gruppen, Norwegian Property, PGS, Statoil and Veidekke, for example, have provided satisfactory explanations to this year's shareholder meetings.

See also the discussion of our dialogue with portfolio companies on page 13.

## OUR PROCEDURES FOR

### PARTICIPATION IN SHAREHOLDERS' MEETINGS

- Folketrygdfondet votes at the shareholders' meetings of portfolio companies.
- Wherever practicable, we aim to participate in person in the meetings of companies listed on the Oslo Stock Exchange.
- If we vote by proxy, we always issue voting instructions.
- Loaned shares will normally be recalled before shareholders' meetings so that we can vote for the full shareholding.
- Prior to a shareholders' meeting, we conduct a thorough review of the agenda and vote in accordance with our principles, guidelines and assessments.
- If we disagree with a board proposal, we seek to explain our position before the shareholders' meeting.
- We normally publish a voting statement on our website after the shareholders' meeting.
- Folketrygdfondet may make proposals to shareholders' meetings, but will in such cases engage in dialogue with the company concerned before submitting any proposal.

From [Folketrygdfondets eierskapsutøvelse \[Folketrygdfondet's active ownership\]](#), June 2012

### OVERVIEW OF COMPANIES WHERE FOLKETRYGDFORNET HAS VOTED AGAINST PROPOSALS FROM THE BOARD OF DIRECTORS\*

Company	Number of cases	Types of cases
Spectrum	5	Option scheme for senior executives** Executive remuneration statement and option programme Authorisation to issue shares under the option programme Authorisation to issue convertible bonds Repurchase of own shares
Lerøy	2	Executive remuneration statement Authorisation to issue shares
RCCL	1	Executive remuneration statement
Atea	2	Executive remuneration statement Authorisation to issue shares under an option programme
Algeta	3	Executive remuneration statement Authorisation to issue shares under an option programme Directors' remuneration in the form of share options
<b>Totalt</b>		
Five companies	12 cases	

\* Folketrygdfondet also voted against shareholder proposals in four companies.

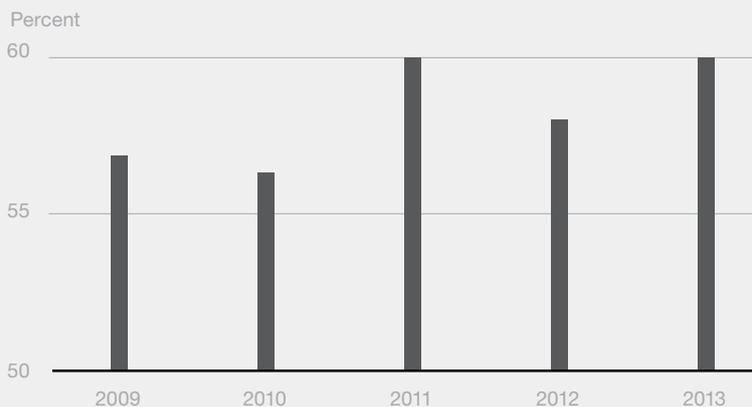
\*\* Extraordinary shareholders' meeting, November 2012

### OUR REASONS FOR VOTING AGAINST EXECUTIVE REMUNERATION STATEMENTS

Company	Voting statement
Algeta	...In Folketrygdfondet's view, option programmes must be approved by the shareholders' meeting, must incorporate clear, performance-related award criteria and an allocation ceiling, and must have a reasonable scope. We cannot see that these factors are reflected in the description of the option programme provided in Algeta's annual report...
Atea	...The executive remuneration statement does not describe the award criteria used in the bonus and share option programme, and the programme has no allocation ceiling...
RCCL	...We consider the scope of the option programme and the total remuneration described in the executive remuneration statement to be unreasonable in view of the results achieved over time...
Lerøy	...The executive remuneration statement does not describe the award criteria used in the bonus and share option programme, and the programme has no allocation ceiling...
Spectrum	...In Folketrygdfondet's view, the scope of Spectrum's option scheme is unreasonable, as it involves the potential issue of new shares totalling 19.9 percent. In Folketrygdfondet's view, the option scheme involves an excessively large transfer of assets from the shareholders to the company's employees...

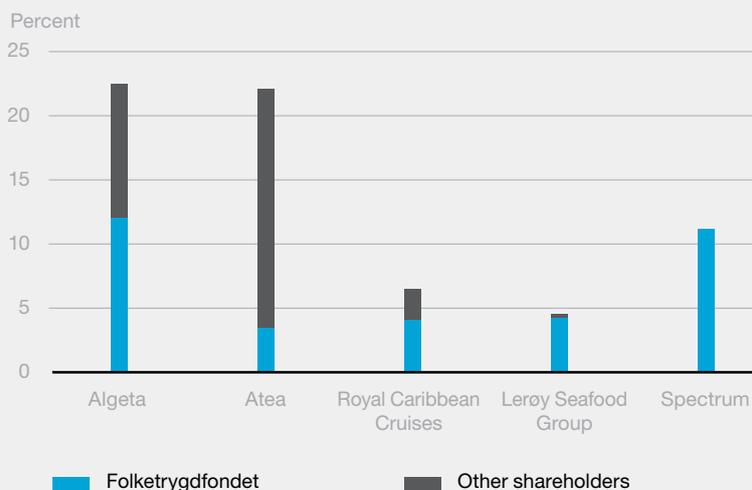
For complete voting statements, see [www.ftf.no](http://www.ftf.no)

AVERAGE ATTENDANCE PERCENTAGE AT SHAREHOLDERS' MEETINGS OF NORWEGIAN COMPANIES IN FOLKETRYGDFONDET'S PORTFOLIO 2009-2013



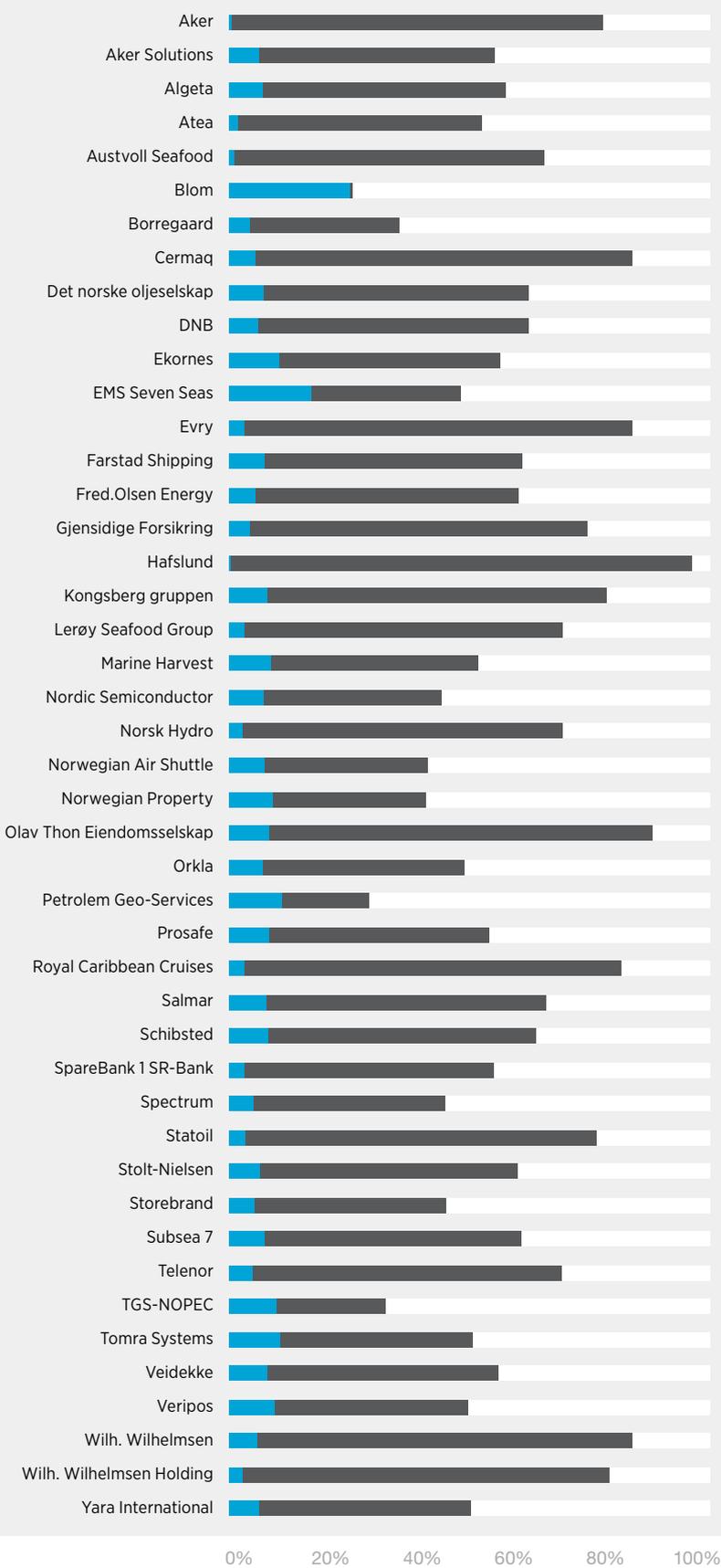
The average attendance percentage at shareholders' meetings of Norwegian portfolio companies has varied between 56.3% and 60% in the last five years.

EXECUTIVE REMUNERATION STATEMENTS OPOSED BY FOLKETRYGDFONDET  
Voting against proposals as a percentage of attending votes, first half of 2013



Folketrygdfondet voted against the executive remuneration statements of five companies. In four of the companies, other shareholders also voted against the executive remuneration statements.

ATTENDANCE AT SHAREHOLDERS' MEETINGS OF NORWEGIAN COMPANIES IN FOLKETRYGDFONDET'S PORTFOLIO, FIRST HALF OF 2013



Folketrygdfondet  
Other shareholders  
Not represented

Attendance at shareholders' meetings has varied between 25.8% and 96.2%.

Folketrygdfondet became a shareholder in the companies Blom and EMS Seven Seas through the conversion of bonds. See discussion on page 28.

Folketrygdfondet attended a total of 45 shareholders' meetings in the first half of 2013.

Folketrygdfondet's share of votes has exceeded its ownership percentage because not all shareholders have been represented at shareholders' meetings. On average, Folketrygdfondet's share of votes totalled 13.9%. In six cases, Folketrygdfondet accounted for more than 20% of the votes.

SHAREHOLDERS' MEETINGS – FOCUS TOPIC:

## THE INCREASING IMPORTANCE OF PROXY AGENTS

Investee companies seek to make it easy to vote at shareholders' meetings. In addition, various service providers such as so-called proxy agents offer analysis services and advice to shareholders on how to vote.

**The Norwegian** Code of Practice for Corporate Governance (NUES) states that the board of a company should facilitate the participation of as many shareholders as possible in shareholders' meetings. Many companies follow this recommendation by enabling shareholders to vote by proxy.

It is difficult for an investor with shareholdings in many companies to assess every matter arising in every company. However, proxy agents simplify the work involved considerably through analyses of agenda items and voting advice. Their analyses are based on national and international rules, practice and corporate governance principles, as well as any guidelines the individual investor may have given. Folketrygdfondet subscribes to and makes active use of such analysis and voting services.

... the recommendations of such proxy agents have a significant impact on Norwegian shareholders' meetings

It is very positive that methods and services have been developed that enable all shareholders to evaluate and vote on matters presented to the shareholders as a group. Such services may be particularly useful to foreign institutional investors who have fewer opportunities to participate in all shareholders' meetings personally or to evaluate all individual matters. Since more than one-third of the shares on the Oslo Stock Exchange are owned by foreign investors, it is reasonable to assume that many employ such analyses. It therefore also seems likely that the recommendations of such proxy agents have a significant impact on Norwegian shareholders' meetings.

However, in our experience, voting based exclusively on such external analyses can be unnecessarily restrictive. If ever more shareholders choose to apply such standardised analyses uncritically, company boards may increasingly be unable to secure support for well-considered, well-founded proposals.

... voting based exclusively on such external analyses can be unnecessarily restrictive

For example, proxy agents may advise against the election of a board candidate holding many directorships, without taking into account whether the nomination committee has already considered the circumstances and deemed them acceptable. Since many investors, and particularly institutional investors, follow such recommendations, proposals may therefore be blocked simply because the rules followed by proxy agents do not take all situations and problems into account. Accordingly, in our opinion it is important for both owners and companies to be aware of the increasing influence of proxy agents.

It is important to emphasise that Folketrygdfondet also benefits greatly from such analyses. We use them primarily to follow up on the shareholders' meetings of Nordic portfolio companies located outside Norway. Since these investments are spread among a larger number of companies and our ownership stakes are smaller, it is more difficult for us to participate actively in shareholders' meetings. Nevertheless, before following the recommendations of a proxy agent, we conduct our own assessment of whether the advice is consistent with our principles.

## SHAREHOLDERS' MEETINGS, NORDIC REGION:

## VOTED AT 108 SHAREHOLDERS' MEETINGS

In the autumn of 2012 and first half of 2013, Folketrygdfondet voted at a total of 108 shareholders' meetings of companies in the Nordic portfolio.

**In total**, we voted on 1,269 matters at shareholders' meetings held in the autumn of 2012 and spring of 2013. We voted against, or abstained from voting on, 33 board proposals. We also voted against, or abstained from voting on, 51 shareholder proposals.

#### Executive remuneration statements

Most of the board proposals we voted against related to executive remuneration statements. We often find that executive remuneration statements contain insufficient information about the schemes, that incentive programmes lack individual performance requirements, and that schemes are highly discretionary. These are our main reasons for voting against executive remuneration statements.

#### Nomination committees and appointment of auditors

In three Swedish companies, the board chair was also proposed as the chair of the nomination committee. In our view, board members should not be represented on nomination committees, and so we voted against each of the proposals.

We have also seen examples where auditors provide additional, non-auditing services to companies and the fees for such additional services exceed the audit fees. In such cases, we have consistently voted against reappointment of the auditors.

#### Shareholder proposals

We often vote against proposals submitted by shareholders because many proposals are not adequately substantiated. Moreover, a number of shareholder proposals have concerned matters that, under general principles for the division of responsibilities within a listed company, fall outside the decision-making powers of the shareholders as a group. Accordingly, we have voted against such proposals.

We only voted for two shareholder proposals during this shareholders' meeting season in the Nordic region. One proposal, which mirrored a proposal made last year, concerned consideration of whether the A and B shares in a company could be assigned equal voting rights. We also voted for a shareholder proposal opposing the reappointment of auditors.

#### Votes at all shareholders' meetings

We have been able to vote at all shareholders' meetings of Nordic portfolio companies since the shareholders' meeting season 2010. We subscribe to an analysis service that enables us to assess the specific matters submitted to shareholders' meetings based on our principles and guidelines. This procedure allows us to vote consistently across the entire equity portfolio.

#### OUR PROCEDURES FOR

#### ACTIVE OWNERSHIP IN THE NORDIC PORTFOLIO

- Folketrygdfondet gives priority to the same ownership issues across the entire portfolio.
- Because we have invested in a larger number of companies, and generally have smaller ownership stakes, in Sweden, Denmark and Finland than in Norway, our active ownership is less intensive in this part of the portfolio.
- In the Nordic region, we primarily exercise our ownership by voting at shareholders' meetings.
- We have access to analyses that enable us to evaluate the individual matters to be voted on at such meetings, and we often appoint an agent to vote for us in accordance with our voting instructions.

From [Folketrygdfondets eierskapsutøvelse \[Folketrygdfondet's active ownership\]](#), June 2012

### VOTING IN THE NORDIC PORTFOLIO, SECOND HALF OF 2012 AND FIRST HALF OF 2013

	Sweden	Denmark	Finland	Total
Total number of shareholders' meetings voted at	67	17	25	109
Total number of matters voted on	805	237	227	1,269

#### Proposals where we have opposed the board recommendation, by topic:

■ Executive remuneration statement	18	1		19
■ Nomination committee – board chair as chair of nomination committee and scrapping of nomination committee	4			4
■ Changes to articles of association	2			2
■ The board/board remuneration	3	1		4
■ Auditors' fees/reappointment of auditors	2		2	4
■ Indemnity for board members	1			1

#### Shareholder proposals

Against	40			40
For	2		1	3

## NOMINATION COMMITTEES AND GOVERNING BODIES:

## PARTICIPATION IN SEVEN NOMINATION COMMITTEES

Folketrygdfondet is represented on the nomination committees of seven Norwegian companies. We also participate in five corporate assemblies and eight shareholders' committees.

**At this year's** shareholders' meeting of Det norske oljeselskap ASA, Nils Bastiansen, Executive Director Equities at Folketrygdfondet, was elected to the company's newly established corporate assembly. Folketrygdfondet voted for the nomination committee's recommendations regarding the board and the corporate assembly, but commented in both cases that the bodies lacked balance in their composition. Folketrygdfondet's voting statement noted that, "... the largest shareholder has received representative weight and influence that are disproportionate to its ownership stake".

Folketrygdfondet also chose to emphasise the board's responsibility to protect the interests of all shareholders in the company.

Folketrygdfondet's involvement in Det norske's newly established corporate assembly will, as underlined in the voting statement, be used to monitor that everyone is working for the interests of the shareholders as a whole.

### The importance of nomination committees

Given its role as financial investor, Folketrygdfondet is not permitted to sit on company boards. However, we engage in board elections, primarily to ensure that the portfolio companies have reliable processes in place for assembling competent boards. Nomination committees have assumed an increasingly central role in recent years. Company boards are becoming more professional, and the election of board members with the right expertise for the company has grown in importance.

Folketrygdfondet has helped to promote this trend, not least through its involvement in the Eierforum group of institutional investors and in relation to the Norwegian Code of Practice for Corporate Governance (NUES). We also give priority to participation in the nomination committees of some portfolio companies, although we have to limit our involvement due to the time-consuming nature of the work.

### OUR PROCEDURES FOR

#### PARTICIPATION IN AND INPUT TO NOMINATION COMMITTEES AND GOVERNING BODIES

- Folketrygdfondet seeks to ensure that portfolio companies have nomination committees.
- Nomination committees must protect the interests of the shareholders as a group and introduce reliable processes for ensuring that the board of directors is composed of people with appropriate, relevant expertise.
- We will give input to nomination committees wherever possible.
- We may participate in the nomination committees of companies in which Folketrygdfondet has a significant shareholding, or when other considerations indicate that it would be appropriate.
- We may also be represented in corporate assemblies and shareholders' committees, although we are not permitted to accept directorships.

From [Folketrygdfondets eierskapsutøvelse](#) [Folketrygdfondet's active ownership], June 2012

### NO BOARD REPRESENTATION

When the Storting (the Norwegian parliament), permitted Folketrygdfondet to invest in shares in response to Proposition to the Storting No. 69 (1990–1991), an upper limit was set on the size of Folketrygdfondet's ownership stakes. Since 1992, the limit for companies listed on the Oslo Stock Exchange has been 15 percent.

The Ministry of Finance emphasised that board representation is not natural given Folketrygdfondet's role as a financial investor. However, Folketrygdfondet may participate in corporate assemblies and shareholders' committees if other shareholders support its involvement.

## FOLKETRYGDFONDET'S REPRESENTATIVES ON NOMINATION COMMITTEES AND GOVERNING BODIES

### Corporate assemblies

Norsk Hydro ASA	Deputy Managing Director Lars Tronsgaard	Member
Orkla ASA *	Managing Director Olaug Svarva	Member
	Portfolio Manager Ann Kristin Brautaset	Member
Statoil ASA	Managing Director Olaug Svarva	Chair
Telenor ASA	Managing Director Olaug Svarva	Deputy chair
Det norske oljeselskap ASA	Director Nils Bastiansen	Member

### Shareholders' committees

DNB ASA	Director Nils Bastiansen	Member
■ DNB Bank ASA		
■ DNB Boligkreditt AS		
■ DNB Næringskreditt AS		
■ DNB Skadeforsikring AS		
■ DNB Livsforsikring ASA		
Gjensidige ASA	General Counsel Christina Stray	Member
Storebrand ASA	Managing Director Olaug Svarva	Member
	Deputy Managing Director Lars Tronsgaard	Deputy member

### Nomination committees

Orkla ASA	Managing Director Olaug Svarva	Member
Schibsted ASA	Director Nils Bastiansen	Member
Statoil ASA	Managing Director Olaug Svarva	Chair
Storebrand ASA	Managing Director Olaug Svarva	Member
TGS-Nopec ASA	General Counsel Christina Stray	Member
Veidekke ASA	Managing Director Olaug Svarva	Member
Yara ASA	Portfolio Manager Ann Kristin Brautaset	Member

\* On 18 April 2013, the shareholders' meeting of Orkla ASA authorised the board of directors to dissolve the corporate assembly. This has now been completed.

## ESG ANALYSES AND FOCUS AREAS:

**TO REDUCE FINANCIAL RISK:** Folketrygdfondet has invested in certain sectors that present particular challenges in relation to environmental, social and corporate governance issues (ESG issues). In response to these challenges, we have developed a risk management tool – ESG analyses – for use in following up on our Norwegian portfolio companies. This tool has allowed us to define a number of special focus areas. Four selected focus areas are presented below.

### Corruption

**Companies in which Folketrygdfondet** invests shall not be involved in corruption. Nevertheless, we see that our portfolio faces a risk of corruption because some companies have operations in countries where corruption is widespread.

Corruption undermines value creation in society and damages the business of the company involved. At the individual company level, the economic consequences of corruption may include exclusion from markets, loss of contracts, fines and extensive legal proceedings.

Corruption can be a difficult issue to deal with, not least because it can take many forms. In addition, companies with international operations may be involved in activities or partnerships in countries where attitudes towards corruption differ from those in their home country. Many Norwegian companies operate in countries ranked high on Transparency International's Corruption Perceptions Index. If a company chooses to invest in such a country, steps must be taken to ensure that it does not become involved in corrupt activities. We understand that this can be challenging, and that engaging in business activity in such countries presents many dilemmas. However, in our capacity as an investor, we cannot accept companies' involvement in corruption, irrespective of where they operate.

Each individual company is responsible for protecting its business, its assets and its reputation against corruption. This requires companies to have guidelines and procedures in place, and to report on their efforts in this area. We have developed anti-corruption guidelines to clarify our expectations of portfolio companies; see page 30.

### Recent example

In the course of the past year (2012 – 2013), suspicions arose that several telecoms companies, including Telia Sonera and Vimpelcom (partly owned by Telenor), were involved in corruption connected to licence agreements in Uzbekistan. The seriousness of the allegations resulted in the resignation of Telia Sonera's chief executive and the launch of a criminal investigation into the company in Sweden. Folketrygdfondet has conducted a dialogue with Telenor to obtain information about the Vimpelcom incident and to review the anti-corruption measures implemented by Telenor. These kinds of measures are intended to preclude similar incidents in Telenor's own operations in countries where the risk of corruption is high.



### Unconventional oil and gas production

**As per 30 June 2013**, Folketrygdfondet owned 3.37% of the shares in Statoil. The shareholding is valued at NOK 13.4 billion, and is the largest single investment in the equity portfolio.

In recent years, Statoil's involvement in unconventional oil and gas production has become relevant to Folketrygdfondet in its capacity as a shareholder. Statoil's activities are attracting considerable attention, due both to the size of the resources and the environmental and social challenges involved in producing them. Stakeholders have also been keen to assess the profitability of such projects in view of the high production costs involved and uncertainty about future oil and gas prices and the level of CO<sub>2</sub> taxes.

Folketrygdfondet has conducted its own evaluation of various risks and opportunities linked to Statoil's oil sand project in Canada and the company's investment in the production of shale gas and tight oil in the USA. As regards the Canadian oil sand project, greenhouse gas emissions are a particular challenge that Statoil needs to overcome to be able to produce the resources in a manner that is both environmentally sound and profitable for investors. As regards the US operations, our questions concern the consumption and recycling of water, methane emissions and the use of chemicals. Gas flaring in connection with the company's operations in North Dakota is also an important topic.

Folketrygdfondet has had several meetings with Statoil on specific challenges related to these investments, and clearly presented its expectations regarding the company's communications in this area. During the past year, Statoil has briefed Folketrygdfondet and other shareholders on how it is dealing with these issues.

Statoil's public reports on its oil sand activities comprehensively document the work it is doing, including its efforts to reduce greenhouse gas emissions from oil sand production, reduce water consumption and make a positive contribution to the local community. Although corresponding reporting on shale gas production in the USA has yet to be finalised, we expect more specific reporting in 2014.



### Human rights and workers' rights

In Folketrygdfondet's experience, human rights and workers' rights are being paid increasing attention as general understanding of the responsibilities of companies and investors in these areas grows.

We are improving our knowledge and expertise relating to human rights and workers' rights, and are discussing these topics with ever more companies. In this context, we have also developed guidelines on human rights and workers' rights based on the UN Global Compact and relevant UN and ILO conventions; see page 30.

As in the case of corruption, these topics are of particular relevance to companies operating in countries marked by poverty and weak or undemocratic political leadership. Many Norwegian companies have operations, partners or suppliers in countries that lack a reliable framework for protecting basic human rights and labour standards. If a company chooses to invest in such a country, it must take steps to avoid contributing, directly or indirectly, to breaches of human or workers' rights. In such cases, it is insufficient for companies to operate in accordance with local regulations. They must also comply with international guidelines and conventions.

In connection with new agreements or investments, companies should conduct due diligence assessments to identify potential risks and challenges related to human rights and workers' rights. As well as identifying risks, they should evaluate whether and how any negative matters can be prevented or reduced.

#### Recent example

Folketrygdfondet has initiated dialogues with Telenor and Subsea 7, among others, to discuss the companies' efforts to promote human rights and workers' rights. This has also been a key topic in the dialogue with Nordic portfolio companies conducted on Folketrygdfondet's behalf by an external service provider. See page 14 for an overview of the dialogues.

#### Climate

**As a long-term investor**, Folketrygdfondet is concerned about how the portfolio companies deal with their greenhouse gas emissions, as it sees that these carry a financial risk.



The UN Environment Programme Finance Initiative (UNEP FI), a global partnership between the UN Environment Programme (UNEP) and the financial sector, describes the financial risk associated with greenhouse gas emissions as a combination of regulatory risk and reputational risk.

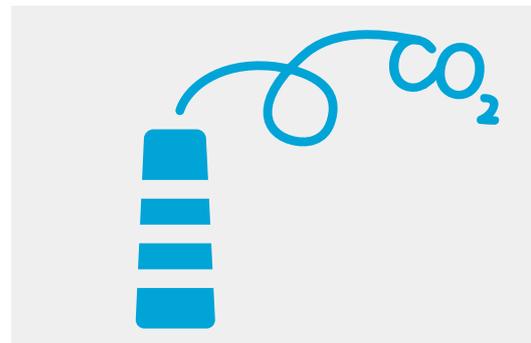
Folketrygdfondet is keen to develop a better understanding of this risk in relation to the individual companies in which it invests. One relevant indicator of climate risk is CO<sub>2</sub> intensity relative to total company sales. Companies engaged in operations with a high CO<sub>2</sub> intensity are more exposed to direct and indirect costs linked to greenhouse gas emissions, such as higher CO<sub>2</sub> taxes, new regulations and customer demands. In 2013, we commissioned a CO<sub>2</sub> analysis of the Norwegian equity portfolio to increase our understanding of climate risk in the portfolio; see the next page.

Market demand for corporate environmental accounts, including reports on energy consumption and greenhouse gas emissions, has increased steadily. We are also seeing new statutory requirements relating to company disclosure related to greenhouse gas emissions, most recently in the United Kingdom. Folketrygdfondet expects portfolio companies to report both internally and externally on how they deal with such issues.

As part of its emphasis on corporate reporting on climate change and CO<sub>2</sub> emissions, Folketrygdfondet has been a participating investor in the Carbon Disclosure Project (CDP) since 2009. Read more about the CDP on page 31.

#### Recent example

During the past year, we have discussed greenhouse gas emissions and reporting with Statoil, Norwegian Air Shuttle, Wilh. Wilhelmsen Holding, Golar LNG, Stolt-Nielsen and Subsea 7.



## FOCUS TOPIC: CLIMATE ANALYSIS

## CO<sub>2</sub> ANALYSIS OF THE PORTFOLIO

Folketrygdfondet is a long-term investor, and must therefore consider the financial risk presented by the portfolio companies' greenhouse gas emissions. This year, to gain a better understanding of climate risk in our investments, we commissioned our first CO<sub>2</sub> analysis of the Norwegian equity portfolio.

**The analysis** of the Norwegian equity portfolio was prepared by the British consulting firm Trucost, and describes:

- The annual greenhouse gas emissions, expressed as CO<sub>2</sub> equivalents (CO<sub>2</sub>e), of the individual companies in the portfolio, weighted by Folketrygdfondet's ownership stake in each company. Trucost's calculations include both direct and indirect emissions. Direct emissions include emissions from operations owned or controlled by a company, while indirect emissions include emissions linked to the purchase of energy and other goods and services.
- CO<sub>2</sub> intensity, i.e. how many tonnes of CO<sub>2</sub>e are emitted relative to company sales aggregated at the portfolio level.

According to the analysis, as per 31 December 2012, Folketrygdfondet's Norwegian equity portfolio was responsible for 4.8 million tonnes of CO<sub>2</sub>e per year. The CO<sub>2</sub> intensity of the portfolio was calculated at 66 tonnes of CO<sub>2</sub>e per million NOK of company sales.

CO<sub>2</sub> intensity is an important indicator because it illustrates the vulnerability of the portfolio with respect to changes in direct and indirect costs linked to

greenhouse gas emissions.

The analysis also showed that several companies in our portfolio are engaged in activities with high CO<sub>2</sub> intensity but do not report on their greenhouse gas emissions.

We would emphasise that the figures set out in the Trucost analysis are only estimates based on the model used by the firm, and that the figures have not been confirmed by the companies. Nevertheless, in our view, the analysis provides useful insights, and we intend to use it when evaluating climate risk at both the company and the portfolio level.

According to the analysis, our investments in the materials, energy, manufacturing industry and consumer goods sectors make the greatest contributions to the portfolio's total CO<sub>2</sub>e emissions. These relatively CO<sub>2</sub>-intense sectors account for a substantial number of the companies listed on the Oslo Stock Exchange, and will therefore also be found in Folketrygdfondet's portfolio.

As in relation to other ownership issues, we will use dialogue with the portfolio companies as an instrument for assuring that the companies are aware of their climate risk and have a strategy and measures in place to manage said risk.

### CALCULATED GREENHOUSE GAS EMISSIONS IN THE NORWEGIAN EQUITY PORTFOLIO

	Number of companies	Investment amount (NOK million)	Total greenhouse gas emissions (tCO <sub>2</sub> e)*	CO <sub>2</sub> intensity (tCO <sub>2</sub> e/NOK million)**
Portfolio	45	76,764	4,809,411	66

The analysis was conducted by Trucost Plc on 23 May 2013, and covers investments in Folketrygdfondet's Norwegian equity portfolio as per 31 December 2012. Information regarding the portfolio companies' financial accounts and greenhouse gas emissions is based on the newest available company data. In this case, this means figures from 2011 or 2012.

\* The total portfolio emissions are based on a calculation of the total direct and indirect CO<sub>2</sub>e emissions of the individual portfolio companies weighted by Folketrygdfondet's ownership stake in each company.

\*\* CO<sub>2</sub> intensity expresses how many tonnes of CO<sub>2</sub>e are emitted relative to company sales aggregated at the portfolio level.

THE FIXED-INCOME PORTFOLIO:

## CLOSER FOLLOW-UP OF ISSUERS

Over the past year, Folketrygdfondet has focused on ensuring greater coherence in its ownership activities. This includes the introduction of a monitoring service for all companies in the fixed income portfolios.

**The role of a bondholder** differs greatly from that of a shareholder. There is usually no contact between the parties as long as the issuer meets its interest and repayment obligations.

However, the bond market has become a more important source of funding for a growing number of businesses in recent years. This has also increased the need for ongoing contact between issuers and bondholders. For example, more companies are making bond-market presentations, mirroring long-standing practice in the stock market. Wherever appropriate, we also seek to coordinate our internal meetings with portfolio companies so that both bond and equity portfolio managers are represented.

### Monitoring and dialogue

In December 2012, we expanded our agreement with an external service provider regarding monitoring and follow-up of the fixed-income portfolios. As a result, Folketrygdfondet's Nordic fixed-income investments are now also being monitored and evaluated by reference to international standards, conventions and guidelines. The service provider is authorised to conduct dialogues with companies in both fixed-income portfolios on Folketrygdfondet's behalf if matters requiring follow-up are discovered.

In our view, the way an issuer handles environmental and social matters makes a statement about credit risk. We therefore aim to improve the integration of ESG analyses into our ongoing credit assessment procedures.

If this approach becomes more common among investors, companies' funding costs may be affected in the longer term.

### Default

Bondholders must particularly be aware of their creditor rights in cases where a company defaults on its loan agreements. Folketrygdfondet participated in nine bondholders' meetings in the past year.

In the last couple of years, Folketrygdfondet has been involved in two complicated financial and industrial restructurings. Final solutions have yet to be found for Folketrygdfondet's investments in the companies concerned – Blom ASA and EMS Seven Seas ASA – which have both implemented bond-to-share conversions. Following the transactions, Folketrygdfondet's ownership stakes are 25% in Blom (8% held by the Government Pension Fund Norway and 17% by the Government Bond Fund), and 17% in EMS (respective holdings of 3% and 14%). In both cases, the purpose of the bond-to-share conversion was to protect the financial interests of the bondholders, and Folketrygdfondet deemed the step appropriate for both companies.

### Active ownership

Folketrygdfondet applies the same principles in all of its active ownership activities. However, our situation requires us to engage more actively in companies where we become shareholders through restructuring and bond conversion. As we are often one of the larger bondholders in such cases, we will also become one of the larger shareholders.

Together with other former bondholders, we will maintain frequent contact with the board of a company in which we have become a shareholder in this way. We will also monitor the company's strategic decisions, and our contact will be closer than the contact we normally have with other companies in which we own shares.

**Well-functioning markets**

In 2013, we have invested in measures to improve the transparency and liquidity of the secondary market. We have sought to promote positive development by engaging in the debate, by being represented on the board of Norwegian Trustee, and by joining the Norwegian Fund and Asset Management Association as an associate member.

There is a particular need for more efficient pricing of bonds. One step taken to develop the secondary market is the establishment of an independent pricing company. Folketrygdfondet supports this initiative. We are also seeking to be consistent in the exercise of our creditor rights and to make our principles in this area generally known.

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## LONG-TERM MANAGEMENT OF FIXED INCOME PORTFOLIOS

The most important objective of our responsible fixed income management activities is to protect our financial interests.

**Long-term and counter-cyclical**

We aim to be a cost-effective, counter-cyclical and long-term fixed income manager. The fixed income portfolios must be characterised by a good risk spread and low risk of capital losses. As a result, we are selective in our investment choices, emphasise orderly investment conduct, and seek to promote a well-functioning market. Our counter-cyclical investment strategy involves increasing risk when risk premiums are high and, correspondingly, reducing risk when risk premiums are low.

**Reliable credit analyses**

We give strong emphasis to conducting reliable credit analysis to reduce risk and avoid defaults in the portfolios.

**Well-functioning markets**

Our counter-cyclical management approach may promote more efficient market pricing, and we support initiatives to improve the functional ability of the market. Perhaps the biggest current problem in the market is a lack of liquidity and unclear bond pricing. In our view, strong loan agreements and the consistent exercise of creditor rights are absolutely vital for the continued proper operation of the credit market.

**Reporting**

We encourage issuers to make thorough, consistent reports to both shareholders and bondholders, including on developments in relevant loan terms.

**Loan requirements**

We are seeking to ensure that loans are announced with suitable loan clauses adapted to the credit risk the loan is assumed to represent. We will not invest in loans unless a trustee is appointed.

**Default situations**

If a payment default or breach of other clauses in a loan agreement occurs, Folketrygdfondet will participate in bondholders' meetings and any restructuring processes. Our starting point is that the ordinary order of priority must be followed. We are also aware of our responsibility to promote good solutions, and may accept the conversion of debt to equity if we believe this to serve our interests over time. Although we will apply our ownership principles in connection with bond-to-share conversions, in such situations our investment will normally require greater involvement.

**Monitoring and ESG analyses**

Environmental, social and corporate governance issues (ESG issues) are integrated into our capital management activities, and influence how much we decide to invest in relevant companies. In our opinion, the way an issuer deals with such issues makes a statement about credit risk. All issuers in the portfolios are covered by a monitoring service that evaluates them by reference to international standards, conventions and guidelines relating to matters such as the environment, human rights and corruption.

## GUIDELINES:

## NEW TOOL

This year, we have developed guidelines to make it easier for the portfolio companies to meet our expectations.

**Folketrygdfondet will be** an engaged but predictable owner. In accordance with our management mandate, we communicate clear expectations regarding corporate governance and how companies handle environmental and social issues.

The portfolio companies are subject to a number of reporting requirements, both statutory requirements and requirements imposed in recommendations and standards that in some cases are voluntary. In our experience, many of the reporting requirements found in recommendations and standards are later enshrined in law. Examples include the provisions in sections 3-3b and 3-3c of the Accounting Act on the requirement to report on corporate governance and social responsibility.

We respect the value of the portfolio companies' time, and therefore seek to make our dialogues regarding ownership issues and social responsibility as efficient and targeted as possible. As a means of clarifying our expectations, we have developed guidelines for companies' work on:

- executive remuneration schemes
- human rights and workers' rights
- the environment
- anti-corruption.

Our guidelines are intended to help illustrate the principles we expect the portfolio companies to adopt, and how we expect them to follow up and report on each area.

The guidelines are based on Folketrygdfondet's responsible investment principles.

Folketrygdfondet complies with internationally and nationally recognised standards for responsible investment activity. Our guidelines for the portfolio companies are therefore founded on the UN Global Compact and the Norwegian Code of Practice for Corporate Governance.

#### The board of directors and senior executives

Responsibility for corporate governance and dealing with social and environmental issues lies with the board of directors and senior executives. Different companies face different challenges, and it is therefore important that the board and senior executives evaluate and assign priority to the problems that are most relevant to their business model and strategy. The board also has a responsibility to implement suitable guidelines, procedures and reporting routines.

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➤ Folketrygdfondet's guidelines on ownership issues and social and environmental responsibility are available on its website: [www.ftf.no](http://www.ftf.no).

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## EXTERNAL INITIATIVES:

## ESTABLISHMENT OF NORSIF

Folketrygdfondet has helped to establish Norsif, the Norwegian forum for responsible and sustainable investment, but has already been a member of several other initiatives for some time.

**Participation in external** initiatives is an important instrument for exchanging information and experience with other investors and keeping up-to-date with new regulations and standards. We also hope to promote the development of best practice by participating in such initiatives.

### International initiatives

**PRI** Folketrygdfondet signed up to the UN-supported Principles for Responsible Investment (PRI) in 2008. The six principles require responsible owners and investors to integrate environmental, social and corporate governance issues (ESG issues) into their management activities. Our status as a signatory to PRI obliges us to report on our implementation of the principles (see [www.ftf.no](http://www.ftf.no)).

**CDP** Folketrygdfondet is also a signatory investor to the Carbon Disclosure Project (CDP). This independent, non-commercial organisation distributes an annual survey to the world's largest listed companies, asking questions about climate change and greenhouse gas emissions. Based on the survey, the CDP has established the world's largest database of information on how companies deal with greenhouse gas emissions. Folketrygdfondet has access to this database and incorporates relevant information into analyses of portfolio companies.

### Norwegian initiatives

Folketrygdfondet participates in the Eierforum group of institutional investors and the Norwegian Society of Financial Analysts, which in turn is involved in the Norwegian Code of Practice for Corporate Governance (NUES). Folketrygdfondet also participated in the Norwegian Institute of Directors.

We collaborate with other shareholders on individual matters when we believe that cooperation serves our financial interests. We may also collaborate with other investors to bolster support for issues we raise with a company.

**Norsif** In 2012, Folketrygdfondet worked actively on the establishment of Norsif, the Norwegian forum for responsible and sustainable investment, which was officially established on 7 January 2013.

Norsif is an independent association of asset owners, managers, service providers and industry associations operating in Norway.

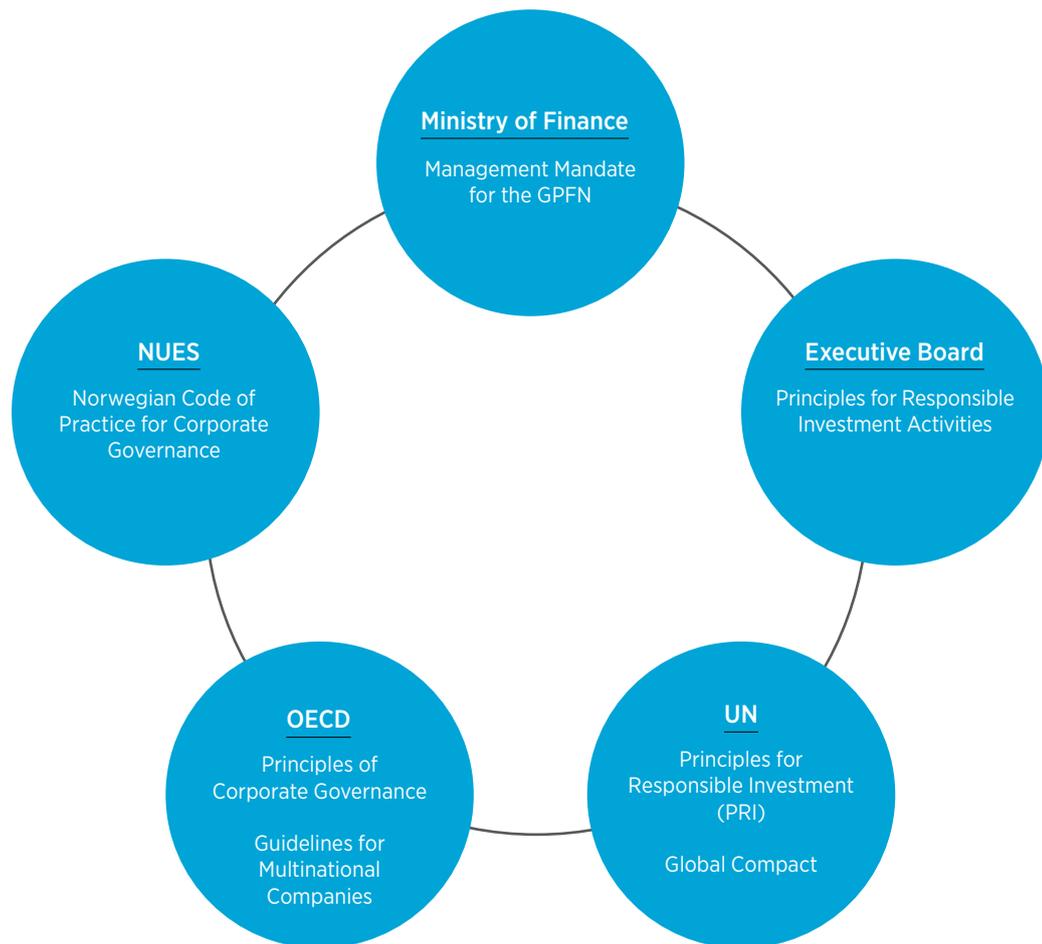
As a professional forum, Norsif aims to promote and contribute to the development of the field of responsible investment and increase awareness of responsible and sustainable investment practices in the Norwegian financial industry and among other stakeholders. Finance Norway (FNO) serves as Norsif's secretariat. See [www.norsif.org](http://www.norsif.org).

### APPOINTMENTS AND PARTICIPATION IN INITIATIVES

Olaug Svarva, Managing Director	Board member, Norwegian Institute of Directors
Christina Stray, General Counsel	Board member, Norwegian Society of Financial Analysts (NFF)
	Member, NUES
	Member, technical committee, Norwegian Institute of Directors
	Member, nomination committee, Norsif
Melanie Brooks, Senior Analyst	Board member, Norsif
Ann Kristin Brautaset, Portfolio Manager	Member, awards committee for the Stockman Prize (awarded by NFF)
Nils Bastiansen, Executive Director Equities	Member, Eierforum
Lars Tronsgaard, Deputy Managing Director	Member, portfolio committee, NFF
	Board member, Norwegian Trustee
Hege Kristine Huse, portfolio manager	Member, bond committee, NFF

In 2013, Folketrygdfondet became an associate member of the Norwegian Fund and Asset Management Association. See the overview of nomination committees and corporate assemblies on page 23.

# MANDATE, GUIDELINES AND PRINCIPLES



## EXCERPTS FROM THE MANAGEMENT MANDATE FOR THE GOVERNMENT PENSION FUND NORWAY\*

**Chapter 2. Responsible investment activities***Section 2-1. Folketrygdfondet's work with responsible management*

- (1) The management of the Fund's capital shall be based on the goal of achieving **the highest possible return**, cf. Section 1-1, Sub-section 2. A good return in the long term is regarded as being **dependent upon sustainable development in economic, environmental and social terms, as well as well-functioning, legitimate and effective markets**.
- (2) Folketrygdfondet shall have internal guidelines for integrating considerations of good corporate governance and environmental and social issues in investment activities, in line with internationally recognised principles for responsible investment. The integration of these considerations shall occur in respect of the GPFN's investment strategy and role as a long-term financial manager.

*Section 2-2. Active ownership*

- (1) Folketrygdfondet's primary goal in its active ownership shall be to **safeguard the GPFN's financial interests**.
- (2) Active ownership shall be **based on the UN Global Compact, the OECD Guidelines on Corporate Governance and the OECD Guidelines for Multinational Enterprises**. Folketrygdfondet shall have internal guidelines for its exercise of ownership rights that indicate how these principles are integrated.

*Section 2-3. Contribution to the development of good national standards for responsible investment and active ownership*

Folketrygdfondet shall actively contribute to **the development of good national standards in the area of responsible investment and active ownership**.

\*) Emphasis added

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