Investment Guidance paper on Governance and Business Ethics

Supporting document to implement the RI Policy Framework

April 2024

NN

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1. Introduction

At NN Group, we aim to conduct our business in a sustainable manner, which includes responsible governance practices. In this guidance paper we focus on our investment approach with regards to governance. The guidance provides background information on governance and explains the due diligence processes that we apply. It also describes what relevant standards and principles currently exist to promote best practices and mitigate negative impact of companies in which we invest.

Background Guidance Papers

NN Group adopted the Responsible Investment Policy Framework in 2014. We define Responsible Investment (RI) as the systematic integration of Environmental, Social, and Governance (ESG) factors into investment decision-making and active ownership practices. Our Responsible Investment Policy Framework reflects our commitment to various international and sector-specific standards and initiatives. A key part of our approach to Responsible Investing is that, where possible and feasible, we aim to mitigate the negative impacts of our investments on sustainability factors. These negative impacts are also called adverse impacts, whereby the most significant adverse impacts are referred to as principal adverse impacts (PAIs). Principal adverse impacts can occur in different areas, such as related to environmental, social and employee matters, human rights, corruption, and bribery.

NN is developing guidance papers which are intended to be a basis for discussion between NN Group and our stakeholders. They are living documents that will regularly be reviewed by NN Group to reflect evolving risks and best practices, as well as solidify our ongoing education on these topics. The guidance papers also help our external asset managers in evaluating investments from a topic-specific perspective. By publishing these papers externally, we aim to express our position and use it to leverage change in the sphere of our investment activities.

NN Group and governance

The basis of our approach to governance is embedded in the NN statement of Living our Values, which provides the foundation on which we do business. The statement says that we strive to 'avoid or responsibly manage any negative impact our business activities may have on people or the environment and seek positive change in society'.

When investing in companies, there is a potential that we become linked to challenging governance related situations. Implementing a due diligence process to incorporate ESG considerations in investment analyses and active ownership practices, will help us to identify, prevent and mitigate sustainability-related risks, including those related to governance practices. In addition, we believe such a process will support us in making better informed business decisions and in identifying sound and beneficial opportunities.

This paper begins with an introduction to the international frameworks and principles that are the foundation of governance. This is followed by an explanation of how companies and industries are exposed to governance risks, illustrated with a risk assessment that we performed. Further, it provides examples of sub-themes which we believe are important in relation to governance.

2. Governance and the role of our investees

International legal and regulatory frameworks

Governance refers to all processes of governing, the institutions, processes and practices through which issues of common concern are decided upon and regulated. Good governance adds a normative or evaluative attribute to the process of governing. While there is no internationally agreed definition of 'good governance', it pertains to the political and institutional processes and outcomes that are necessary. When good governance principles are not applied, there can be significant risks and negative consequences. These can include:

- Corruption: Corruption can become endemic, with public officials using their power for personal gain and engaging in bribery, embezzlement, and other corrupt practices. This can undermine public trust in government and lead to a loss of legitimacy.
- Inefficiency: Government institutions may be inefficient and ineffective, with limited capacity to deliver public services or respond to the needs of citizens. This can lead to frustration and disillusionment among the population, and can also hinder economic development.
- Human Rights Violations: There is a risk of human rights violations, including the abuse of power, discrimination, and the suppression of political opposition. This can lead to social unrest, conflict, and even violence.
- Lack of Accountability: There may be a lack of accountability and transparency in government decision-making, with officials operating in secrecy and without oversight. This can lead to a lack of trust in government and public institutions.
- Environmental Degradation: There may be a disregard for environmental protection and sustainability, leading to pollution, deforestation, and other forms of environmental degradation.

Understanding the international regulatory frameworks and principles that serve as the foundation of governance is essential to grasp the role of companies and countries in promoting good governance. There are many different laws and regulations in place, including several international regulations, as well as regional and local laws. The most well-known international laws, guidelines and conventions that focus on governance related topics include:

- **United Nations Development Program principles of good governance**: These principles of good governance are designed to help promote democratic and accountable systems of government that are responsive to the needs and concerns of all members of society. See the box on the page before for more details.
- **United Nations Convention against Corruption**: This convention, adopted in 2003, is a legally binding agreement that requires countries to take measures to prevent and combat corruption, including bribery, money laundering, and embezzlement.
- **OECD Anti-Bribery Convention:** This convention, adopted in 1997, requires member countries to criminalize bribery of foreign public officials and to put in place measures to prevent and detect such bribery.
- **Financial Action Task Force (FATF) Recommendations:** The FATF is an intergovernmental organization that sets global standards for combating money laundering, terrorist financing, and other threats to the international financial system. Its recommendations provide guidance to countries on how to prevent and detect money laundering and other financial crimes.

Additionally, regional organisations, such as the **OSCE (Organization for Security and Co-operation in Europe)**, have made decisions aimed at promoting good governance and combating corruption, money-laundering, and the financing of terrorism within its participating States. As part of its mandate, the OSCE works towards conflict prevention, crisis management, and post-conflict rehabilitation in the region of Europe, Central Asia, and North America. The OSCE has made ministerial and permanent council decisions that call on participating States to take measures to prevent and combat corruption, including through the establishment of effective anti-corruption policies, laws, and institutions. The 2014 Basel Ministerial Council Decision on the Prevention of Corruption and the 2012 Dublin Ministerial Council Decla-ration on Strengthening Good Governance and Combating Corruption, Money-Laundering and the Financing of Terrorism provide guidelines for participating States to ensure transparency and accountability in government and prevent financial crimes that threaten regional stability and security.

Principles of good governance

The United Nations Development Program's (UNDP) principles of good governance are:

- Participation: Participation of all members of society, particularly those who are most affected by policies and decisions, is essential to good governance. This principle aims to ensure that all voices are heard, and that decision-making is inclusive and transparent.
- Rule of Law: The rule of law is essential to good governance as it ensures that laws are fair, impartially enforced, and protect human rights. This principle aims to ensure that everyone is equal before the law and that no one is above the law.
- Transparency: Transparency is essential to good governance as it ensures that decision-making is open, accountable, and free from corruption. This principle aims to ensure that information is freely available to the public and that decision-making processes are clear and understandable.
- Responsiveness: Responsiveness is essential to good governance as it ensures that policies and decisions are made in a timely and effective manner. This principle aims to ensure that the government is responsive to the needs and concerns of all members of society.
- Consensus Orientation: Consensus orientation is essential to good governance as it ensures that policies and decisions are made through a process of consultation and dialogue. This principle aims to ensure that decisions are made in a way that reflects the views and interests of all members of society.
- Equity and Inclusiveness: Equity and inclusiveness are essential to good governance as they ensure that everyone has equal access to opportunities and services. This principle aims to ensure that policies and decisions are made in a way that promotes social justice and reduces inequalities.
- Effectiveness and Efficiency: Effectiveness and efficiency are essential to good governance as they ensure that policies and decisions are implemented in a timely and cost-effective manner. This principle aims to ensure that resources are used efficiently, and that policies and decisions achieve their intended goals.

Companies and corporate governance

Effective public governance involves managing and controlling public bodies, with a focus on transparency, accountability, integrity, and risk management. It aims to ensure that public funds are used efficiently, corruption is eliminated, and public bodies perform better. Good governance, on the other hand, covers both public and private sector organisations. It involves clear rules and principles that promote better decision-making and efficient use of resources. It is essential for the sustainability of resources and operations in any organization.

Corporate governance specifically focuses on the mechanisms of governance within corporations. This includes overseeing the allocation and distribution of resources, as well as decision-making processes. It holds management accountable for creating efficiency and value, and make them responsible for distributive decisions that override market allocations.

The foundation of corporate governance lies in establishing a framework of rules, processes and principles to ensure that a company is managed in an effective, efficient and ethical manner. At its core, corporate governance is based on the principles of accountability, transparency, and fairness. In addition to the principles of accountability, transparency, and fairness, corporate governance is also guided by various regulations and guidelines. These regulations and guidelines are designed to ensure that companies are accountable to their stakeholders, and that they operate with integrity, transparency, and fairness.

The specific regulations and guidelines that apply to corporate governance can vary by country and industry, but some common examples include:

- Company Law: This sets out the legal framework for companies, including the requirements for corporate governance, such as the duties of directors, shareholder rights, and financial reporting requirements.
- Regulatory Requirements: These are specific requirements set by regulatory bodies, such as financial regulators, to ensure that companies comply with specific laws and regulations, such as anti-money laundering regulations, data protection laws, or environmental regulations.
- Stock Exchange Listing Rules: These are rules set by stock exchanges that companies must comply with in order to list on the exchange. These rules often include requirements for corporate governance, such as the composition of the board of directors, the role of independent directors, and disclosure requirements.
- Codes of Corporate Governance: These are guidelines that set out best practices for corporate governance. They are often developed by industry associations or regulatory bodies, and can cover a wide range of issues, such as board composition, risk management, and stakeholder engagement.

Governance in NN's investment process

NN Group is committed to responsibly invest our assets. We incorporate environmental, social and governance (ESG) risks and opportunities factors into the investment process, including both ESG-related financial risks (sustainability risks) and adverse impacts on ESG factors of our investment decisions. Our Responsible Investment Framework Policy explains how we incorporate ESG factors into our investment process.

To adhere to our Responsible Investment Framework Policy, we have developed norm-based RI criteria that reflect relevant laws, our values, and internationally recognised standards such as the as the UN Global Compact principles, the UN Guiding Principles on Business and Human Rights, and the OECD Guidelines for Multinational Enterprises.

One crucial aspect of our norm-based RI criteria is our expectation that companies and governments in which we invest adopt and implement appropriate policies and practices to meet internationally recognised governance standards. Based on international guidance and regulations, there are several criteria that we can assess in order to understand whether a company has properly established its governance policies and commitments:

- Transparency: Companies are expected to be transparent about their operations, financial performance, and decision-making processes.
- Accountability: Companies are responsible for their actions, and they should be held accountable for any wrongdoing.
- Fairness: Companies should treat all stakeholders fairly, including customers, employees, shareholders, and suppliers.
- Responsibility: Companies should take responsibility for their impact on the environment, communities, and society at large.
- Compliance: Companies are expected to comply with all relevant laws and regulations.
- Ethics: Companies should operate with integrity and adhere to ethical principles in all their dealings.
- Board oversight: Companies are expected to have a strong board of directors that provides oversight and guidance on corporate strategy and decision-making.

Good governance is also a crucial factor for governments to function effectively and serve the needs of their citizens. It involves upholding the rule of law, promoting transparency and accountability, encouraging citizen participation, being responsive to the needs of citizens, operating efficiently and ethically, protecting human rights, promoting sustainable development, and maintaining political stability. By adhering to these principles, governments can improve the quality of life for their citizens and promote overall societal well-being.

3. Understanding governance risks and impacts

A strong understanding of governance-related risks allows us to identify investment risks and opportunities and to focus dialogue and engagement on the topics that are relevant to the companies in which we invest. While all companies are exposed to some degree of governance risks, the types of risks companies face, and severity and likelihood of occurrence of these risks will vary depending on their sector, operational and supply chain circumstances.

NN's Responsible Investment team conducted an assessment based on governance-related incidents and controversies related to companies' activities. This assessment is based on data points retrieved from our external ESG data provider Sustainalytics, who base their research on public information. The analysis has not been limited to NN Group's investment universe. Instead, we assessed the entire investment universe that was made available to us, we therefore note that not all sectors and issues are fully covered. This approach was taken to ensure a comprehensive perspective on governance risks and impacts. The data points provided relate to the involvement (both through direct operations and their supply chains) of companies in incidents and controversies across the following governance topics:

- Bribery and corruption
- Intellectual property
- Accounting and taxation
- Business ethics
- Corporate governance
- Lobbying
- Anti-competitive practices
- Data privacy and security
- Quality and safety
- Media ethics

Our assessment involved an analysis of the severity of the impact of incidents on society and the environment, as well as the level of financial risk posed to the company. Additionally, we evaluated the probability of a company within a specific industry getting involved in a severe incident. For each topic, the above metrics for company's own operations and its supply chain, as well as for company's adverse impacts and risk exposure was taken into account in a calculation.

Examples of key risks

Consumer Staples: Consumer staples companies are responsible for ensuring the safety of their products. However, in some cases, companies have been found to have failed to meet safety standards, resulting in product recalls and damage to their reputation. The sector also relies heavily on global supply chains, which can be complex and difficult to manage, and they have faced supply chain disruptions as a result. In addition, the sector has come under scrutiny for their labour practices, including low wages and poor working conditions. Finally, the consumer staples sector has had issues with effective corporate governance, lack of board oversight and corruption.

Energy: The energy sector has faced a range of governance issues. Regulatory capture is one such issue, where regulatory agencies become too closely aligned with the interests of the companies they are supposed to be regulating, leading to a lack of oversight and potential abuse of power. Corruption is another issue, with energy companies being accused of engaging in corrupt practices, such as bribery, to secure contracts and favourable treatment from government officials. Environmental concerns are also pressing, with the energy sector under increasing pressure to address issues such as climate change, air and water pollution, and resource depletion. Transparency is yet another issue, with the need for greater transparency in the energy sector, particularly around pricing and supply chains, to ensure that consumers and stakeholders have access to accurate information.

Telecommunication Services: The telecommunications services sector has faced a number of governance issues over the years. These issues include privacy and data protection concerns related to the collection and use of customer data, allegations of monopolistic behaviour and lack of competition, cybersecurity risks and data breaches, net neutrality violations, quality of service issues such as dropped calls and network outages, and corporate governance issues such as executive compensation and board independence. These issues have led to regulatory scrutiny, consumer complaints, and shareholder activism. Effective management and oversight of these governance issues are important for maintaining the trust of customers, regulators, and other stakeholders.

Table 1: Governance Sector Matrix

	Own Operations	Supply Chain
Consumer Discretionary	Medium	Medium
Consumer Staples	High	High
Energy	High	High
Financials	High	Medium
Healthcare	Medium	Low
Industrials	Low	High
Information Technology	Low	Medium
Materials	Low	Low
Real Estate	Low	Low
Telecommunication Services	High	Low
Utilities	Medium	High

The assessment indicates that companies operating in the Consumer Staples, Energy, Financial, Industrials, Utilities and Telecommunication Services sectors have a high risk of governance-related impacts or risks through their own operations and/or supply chain.

We note that the analysis we conducted also indicates low ratings in some sectors such as real estate. However, low ratings do not mean that there are no incidents or risks present. It could be because the outcomes of the assessment are limited by the extent of the company universe as defined by the ESG rating provider, the availability of publicly available incidents and controversies data as well as the premise that (individual) incidents might not necessarily directly impact the risk-profile of a sector or company.

It should also be kept in mind that the assessment is based on historical data at a specific point in time (February 2024), so it is important to update the analysis regularly as new incidents emerge and are resolved. Finally, it is essential to remember that the governance profile will vary from company to company. An analysis of a company's governance performance should therefore always be carried out at the individual company level.

4. Important governance topics and trends

In this chapter, we discuss several governance related issues which we believe are important to address, as well as certain trends that have developed over the years and will play a crucial role in tackling governance failures.

Bribery and Corruption

Bribery and corruption refer to the act of giving or receiving something of value in exchange for a favour or an advantage that is not deserved. The bribe is usually given to influence the behaviour of the recipient and to gain an unfair advantage. Bribery and corruption can occur in many areas, including business, politics, and government. These practices are illegal and can result in severe consequences for those involved, including fines, imprisonment, and damage to reputation. Many countries have laws and regulations in place to prevent and punish bribery and corruption.

In the United States, for example, the Foreign Corrupt Practices Act (FCPA) prohibits U.S. companies and individuals from bribing foreign officials to obtain or retain business. The FCPA also requires companies to maintain accurate books and records and to implement adequate internal controls to prevent bribery and corruption. Similarly, the United Kingdom has enacted the Bribery Act, which makes it illegal to offer, promise, or give a bribe, as well as to request, agree to receive, or accept a bribe. The Bribery Act applies to both individuals and organisations, and companies are required to implement adequate procedures to prevent bribery and corruption.

Many other countries, including Canada, Australia, and EU countries, have also enacted laws and regulations aimed at preventing bribery and corruption. In addition to national laws, many companies also adhere to international standards such as the United Nations Global Compact or the OECD Guidelines for Multinational Enterprises, which provide guidance on ethical business practices and promote anti-corruption measures.

Despite the different laws and regulations, bribery and corruption still occurs frequently. There have been several high-profile cases of bribery and corruption by companies in recent years. One of the most notable cases involved the Brazilian construction company Odebrecht, which was involved in a massive bribery scheme that spanned several countries in Latin America and Africa. The company paid bribes to government officials and political parties in exchange for contracts and other favours.

In another case, the Swedish telecommunications company Ericsson was fined USD 1 billion by the U.S. Department of Justice for bribery and corruption in several countries. The company admitted to paying bribes to government officials in China, Vietnam, and Djibouti to win contracts. Other companies that have been implicated in bribery and corruption scandals include the German carmaker Volkswagen, which was fined USD 4.3 billion in the U.S. for cheating on emissions tests, and the British multinational bank HSBC, which was fined USD 1.9 billion for laundering money for drug cartels and other criminal organisations.

These cases highlight the significant impact that bribery and corruption can have on companies, including financial penalties, damage to reputation, and loss of business. They also underscore the importance of strong anti-corruption measures and ethical business practices to prevent such conduct from occurring. NN strictly prohibits the offering or accepting of bribes. Employees may not engage in any activity that may give the appearance of offering or accepting a bribe.

Case: Controversy engagement

NN Group has established norms-based RI criteria that focus on governance, human rights, labour, environment, and bribery and corruption. These criteria are considered a minimum requirement for managing proprietary assets. When a company severely and structurally breaches these criteria, NN Group initiates a formal engagement process.

The Controversy and Engagement Council oversees NN Group's direct, collaborative, and delegated engagement activities. The council meets quarterly to monitor progress on engagement activities and determine necessary steps to achieve engagement objectives at individual company level. The Council provides inputs and recommendations to the RI Committee, which validates whether engagement remains feasible or if a company should be added to the NN Group Restricted List. Potential violations of NN Group's norms-based RI criteria can be raised by external ESG research or engagement providers, input from asset managers, information from NGOs or media sources, and NN Group staff research. If the Council determines that engagement to address violations is feasible, the company will be included in NN Group's engagement programme and can be engaged directly or through external asset managers or engagement service providers.

Money Laundering

Money laundering is the process of disguising the proceeds of illegal activity as legitimate funds. It involves transferring money through a complex series of transactions to hide its origin and make it appear as if it came from a legal source. The aim of money laundering is to make the illegal proceeds appear clean and to avoid detection by law enforcement agencies.

Money laundering can be used to conceal the proceeds of various illegal activities, such as drug trafficking, fraud, or terrorism. It can involve multiple transactions through various financial institutions and across different countries. It is a serious crime and is punishable by law. Governments and financial institutions have implemented various measures to prevent and detect money laundering, including the use of anti-money laundering (AML) regulations, Know Your Customer (KYC) requirements, and other measures aimed at detecting suspicious financial activity.

Money laundering is a widespread problem that affects many countries and industries. There are some high-profile examples of where either companies or governance were involved:

- The 1MDB scandal in Malaysia, in which billions of dollars were embezzled from a government investment fund and laundered through various channels.
- The Danske Bank scandal in which over USD 200 billion in suspicious transactions flowed through the bank's Estonian branch between 2007 and 2015.
- The Russian Laundromat, a massive money laundering scheme that involved the creation of fake companies and the use of fraudulent loans to move money out of Russia and into the global financial system.

NN's approach to Financial Economic Crime

NN Group is committed to combatting Financial Economic Crime to protect society and customers from criminal activities such as money laundering, financing terrorism, and breaching sanctions regimes. Our Financial Economic Crime Policy outlines mandatory minimum requirements to detect and prevent Financial Economic Crime based on applicable laws and guidelines. This policy requires implementation of customer and business partner due diligence processes, including sanction checks and where applicable, Ultimate Beneficial Ownership (UBO) and, Politically Exposed Persons (PEPs) checks to avoid engaging in business with individuals or entities assessed as an unacceptable risk. We have appointed FEC Compliance Officers in all business units to monitor compliance with these policies this policy and train employees to detect and report FEC risks and expect them to report incidents.

- The Wirecard scandal in Germany, in which the payments company was found to have inflated its revenues and profits, while also engaging in money laundering and other fraudulent activities.

Responsible Taxation

Responsible taxation refers to the idea that individuals, businesses, and governments should pay their fair share of taxes in a transparent and ethical manner. This includes paying taxes on income, profits, and other sources of revenue, as well as complying with tax laws and regulations. It is important because it helps to ensure that government programs and services are adequately funded, and that everyone is contributing their fair share to society. It also helps to prevent tax evasion and other forms of financial crime, which can undermine the integrity of the tax system and harm the economy.

Some examples of responsible taxation practices include:

- Paying taxes on time and in full and keeping accurate records of income and expenses.
- Complying with tax laws and regulations and seeking professional advice when necessary.
- Being transparent about tax planning strategies and avoiding aggressive tax avoidance schemes.
- Supporting efforts to combat tax evasion and other forms of financial crime.

NN's approach to Taxation

At NN Group, we believe that being a responsible taxpayer is part of good corporate citizenship. We see taxes as a contribution to society in the countries in which we operate. Further, we recognize that taxes are vital for sustainable development of people and planet, either as a source of income to finance the transformation or as an instrument to influence behaviour.

NN Group is transparent about its approach to tax and the tax positions, and we expect the same from the companies in which we invest. Disclosures should be made in accordance with international reporting requirements and standards, as well as relevant local regulations. Companies should also be committed to comply with both the letter and the spirit of the tax laws and regulation of the countries in which they operate, and not undertake or engage in arrangements of which the sole purpose is to create a tax benefit. More information can be found on our website.

County Embargoes

An embargo is a government-imposed restriction on trade or economic activity with a particular country or group of countries. Embargoes are often used as a diplomatic tool to put pressure on a country to change its policies or behaviour. They can be comprehensive, prohibiting all trade with a country, or targeted, focusing on specific goods or services, and they are typically imposed for political or security reasons, such as to encourage a country to comply with international law, to prevent the spread of nuclear weapons, or to stop human rights abuses. They can also be used to punish a country for engaging in aggressive behaviour or supporting terrorism.

These restrictions can have significant economic consequences for both the target country and the countries imposing the embargo. The targeted country may experience a decline in trade and investment, while the countries imposing the embargo may lose access to a valuable market.

Embargoes are regulated by international law, including the United Nations, the European Union, and the World Trade Organization (WTO). Countries that impose embargoes must comply with these regulations, and violations can result in economic sanctions or other penalties.

NN Group follows the relevant sanction laws and regulations in our Financial Economic Crime (FEC) policy (refer to case box on page 10). The FEC Policy also sets out our principles on dealing with Ultra High-Risk Countries. NN has business reasons for avoiding transactions with people and entities from some specific countries. NN companies cannot enter into new relationships with customers from these countries and have processes to discontinue any existing relationships or positions involving these countries. In addition, our Responsible Investment Framework policy restricts investing in sovereign bonds from countries with a UN arms embargo. We may also restrict sovereign bond investments for other reasons on a case-by-case basis.

The United Nations Security Council (UNSC) has imposed countrywide arms embargo sanctions on North Korea, Iran, and Libya in recent years. The embargo on North Korea prohibits the sale or transfer of all weapons, except for small arms and light weapons. The embargo on Iran was lifted in 2020 as part of the Joint Comprehensive Plan of Action (JCPOA) but was reimposed by the United States in September 2020. The arms embargo on Libya was imposed in 2011, in response to the violent crackdown on protesters by the Libyan government and has been extended several times since then. The UNSC may also impose targeted arms embargoes on specific individuals or entities in addition to countrywide embargoes.

Case: Supply of Arms

NN considers the trade of arms to certain countries or non-state actors as controversial, due to the high risk that these arms will be used to commit severe human rights violations or prolong conflict. Companies are identified if they are involved in activities in making weapons, weapons systems, or related materiel or services available to countries in which there is a serious risk that the weapons can be used for internal repression, serious violations of human rights or for any other purpose which cannot reasonably be considered consistent with normal and legitimate national security and defence.

We restrict companies that demonstrably have activities in making weapons, weapon systems, or related materiel or services available to (i) countries that are subject to a UN or EU arms embargo that is targeting the central government or (ii) non-state actors sanctioned by the UN or EU. Not in the scope are companies that have such activities in relation to humanitarian missions or to (peacekeeping) military missions that have been commissioned by the international community.

Corporate Governance

Corporate governance involves the systems, processes, policies, and practices used to direct and control a company's operations. It aims to ensure responsible and ethical behaviour among management, directors, shareholders, and stakeholders. Good corporate governance is essential for long-term success, building trust with investors, customers, and stakeholders. It ensures accountability, compliance with legal and regulatory requirements, and emphasizes transparency, fairness, and responsibility.

Corporate governance is regulated by laws, regulations, and guidelines that ensure responsible and ethical company operations. In most countries, legal and regulatory requirements set minimum standards for board composition, financial disclosure, and shareholder rights. Companies may also adopt additional guidelines and best practices, such as codes of conduct and policies for risk management, to promote transparency, accountability, and responsible decision-making.

Good corporate governance is critically important for investors, as it helps to establish trust and confidence in a company. A company with strong corporate governance practices is more likely to be transparent in its operations, accountable for its actions, and responsible in its decision-making processes. This can help to reduce the risk of fraud, mismanagement, and other unethical or illegal activities that can harm investors. Investors are also more likely to support companies with good corporate governance practices, as they are seen as being more likely to achieve long-term success.

Case: Proxy voting

NN's voting activities are focused on three main issues: board elections, alignment of executive remuneration with company strategy, and integration of sustainability within company strategy. NN Group prioritises these issues as crucial factors for the long-term success and stability of companies.

Board elections

Appointing capable directors and creating a diverse, independent board is critical for the performance of a company. While we often support a company's nominees, we vote against them when we think that adding them to the board would detract from the goals of independence and diversity. We may also hold the board accountable for insufficient oversight of environmental and social risks, failure to disclose reduction targets for greenhouse gas (GHG) emissions, and where there are serious breaches of our RI criteria.

Remuneration

Executive pay and the effectiveness and complexity of companies' remuneration policies are recurrent subjects of heated discussion at AGMs. In Europe, there is a broader debate on high levels of compensation for executives in the context of glaring income inequality. In addition, issues such as sustainability, employee health and safety, company goals and management's ability to manage crises are increasingly being factored into decisions on compensation.

Integrating sustainability into long-term strategy

To ensure long-term performance for shareholders, NN Group expects that investee companies act in a responsible way to all stakeholders. This includes recognising the impact of their business decisions on the environment, as well as the social and human rights issues that may arise within the regions and supply chains where they operate. Companies should also indicate which sustainability risks are most material to their business, and how it is aligned with the strategy and accompanying objectives and targets.

Our Voting Policy for Proprietary Assets has more details.

Proxy voting is a crucial tool that investors can use to promote better corporate governance practices. It allows shareholders to exercise their voting rights and influence the decision-making process of a company, thereby holding management accountable for decisions made in the best interests of the company. By using proxy voting, shareholders can approve or reject critical corporate governance issues such as the election of directors, executive compensation, and changes to the company's articles of association. In this way, shareholders can help to promote good corporate governance by ensuring that the company has a strong and effective board of directors, that executive pay is aligned with performance, and that the company's articles of association reflect best practices in corporate governance. Refer to the case box below on how NN Group uses its proxy voting rights.

Business Ethics

Business ethics refers to the moral principles and values that guide behaviour in the business world. It involves making decisions that are not only legal and financially sound, but also socially responsible and ethical. It covers a wide range of topics, including corporate social responsibility, workplace diversity and inclusion, fair labour practices, environmental sustainability, and anti-corruption measures, among others.

Some common ethical dilemmas in business include conflicts of interest, insider trading, bribery, discrimination, and environmental pollution, among others. Adopting ethical business practices can have a positive impact on a company's reputation and bottom line, as well as contribute to a more sustainable and just society. Many companies have developed codes of ethics, established ethical training programs for employees, and implemented sustainability practices as part of their business operations.

There are regulations when it comes to business ethics, and governments around the world have enacted laws and regulations to ensure that businesses operate ethically and responsibly. These regulations may cover a wide range of areas, such as labour practices, environmental protection, consumer protection, and anti-corruption measures.

There have been many high-profile cases related to business ethics over the years. One of the most infamous cases of corporate fraud was Enron, a major energy company that collapsed in 2001 after it was revealed that its executives had engaged in accounting fraud to hide billions of dollars in debt. In 2015, Volkswagen was caught using software to cheat on emissions tests for its diesel cars, leading to billions of dollars in fines and settlements and damaging the company's reputation. Wells Fargo was found in 2016 to have opened millions of fraudulent accounts in order to meet sales targets, leading to the resignation of the bank's CEO and a USD 185 million settlement with regulators. Theranos was a healthcare startup that claimed to have developed a revolutionary blood testing technology, but it was later revealed that the technology did not work as advertised, and the company's founder was charged with fraud.

Political Contributions

Political contributions are donations made by companies to political parties, candidates, or campaigns. These contributions may take the form of cash donations, in-kind contributions, or other types of support, such as providing goods or services to a political campaign.

Contributions by companies are governed by a range of laws and regulations, which vary by country and jurisdiction. In many countries, there are strict rules regarding political contributions, including limits on the amount that companies can donate, disclosure requirements for political contributions, and restrictions on the types of entities that can make political contributions. For example, in the United States, political contributions by companies are governed by the Federal Election Campaign Act (FECA) and other laws and regulations. Under FECA, companies are prohibited from making direct contributions to federal candidates, political parties, or political action committees (PACs). However, companies may establish separate segregated funds (SSFs), also known as PACs, which can make contributions to political candidates or campaigns.

In other countries, such as the United Kingdom, companies are required to disclose political contributions in their annual financial statements, including details of the recipient and the amount donated. The rules governing political contributions by companies in other countries may vary depending on the specific legal and regulatory framework in place.

Investors often engage with companies on political contributions as part of their strategy to promote good corporate governance and social responsibility. These engagements may include shareholder proposals, and voting on resolutions related to political contributions at a company's AGM. Political contributions are considered a risk to companies, and investors believe that engagement on this issue can promote transparency, accountability, and responsible corporate behaviour.

NN's Code of Conduct

NN has three core values: care, clear, commit. Our values, which we published under the title NN statement of Living our Values, set the standard for conduct and provide a compass for decision making. The NN Code of Conduct outlines our position on a number of important topics and lists clear rules of conduct. These rules of conduct are minimum standards to which we must adhere at all times. Some NN businesses may have implemented their own, specific rules of conduct in addition to this Code. If applicable, those rules are laid down in a supplement that is specific to your business.

The statement of Living our Values includes the requirement that employees comply with applicable laws, regulations and internal policies and guidelines. The Code of Conduct and supplements in use in the relevant businesses are an important part of this set of rules. As a result, they apply to every NN employee and anyone representing NN in any capacity (from now on: employees), and we expect all to be familiar with them and live up to them. The Code of Conduct outlines our views and expectations related to:

1. How we interact
2. How we deal with information and (personal) data
3. How we deal with conflicts of interest, fraud, financial economic crime and competition law
4. How we use equipment and the Internet
5. How we report breaches
6. How we deal with breaches

For more information see our website.

Cyber security governance

Cybersecurity refers to the measures taken to protect their computer systems and sensitive data from unauthorized access, theft, damage, and other cyber threats. Some of the common cybersecurity measures include firewalls, antivirus software, intrusion detection and prevention systems, encryption, multi-factor authentication, and regular backups of important data.

In addition to these technical measures, cybersecurity also involves educating employees about cyber threats and best practices for staying safe online. This may include regular training sessions, phishing simulations, and policies around password management and data handling.

Cybersecurity is important for an investor like NN, because it can have a significant impact on the financial health and reputation of the companies we invest in. Cyber threats such as data breaches, ransomware attacks, and other types of cybercrime can result in costly financial and legal consequences, damage to brand reputation, and loss of customer trust.

We need to be aware of these risks and evaluate how well companies are prepared to prevent and respond to cyber threats. A company with strong cybersecurity measures in place is less likely to suffer a major data breach or other cyber-attack, which could have negative consequences for its stock price and overall financial performance.

Case: Cyber security

Meta Platforms (Meta) has been involved in multiple allegations of insufficient measures and management to protect users' data privacy. These incidents include allegations that it was mining data from users' private messages to sell to advertisers as well as sharing data with third parties without users' consent.

Via our external engagement provider, we are participating in an engagement with the company. Over the period of the engagement Meta has not shown a trend of responsiveness to the requests for dialogue, the company's responsiveness to other investor initiatives has also not always been open. This outcome, alongside serious questions around shareholder independence, raises concerns about Meta's interest in considering stakeholder interests and views. With that said, Meta's preparedness to manage its privacy risks and adverse impacts has improved. We will continue to monitor the engagement and the company, to ensure alignment with our norms.

5. Concluding remarks

NN's Responsible Investment Policy Framework highlights the measures we will take to integrate sustainability factors in the investment decision making and active ownership practices. NN has developed norms-based RI criteria, including governance, that are a reflection of relevant laws, the organisation's values, and internationally recognised standards such as the UN Global Compact, the UN Guiding Principles on Business and Human Rights, and the OECD Guidelines for Multinational Enterprises. In case there are strong indications that an issuer may be in violation of any of NN's norms-based RI criteria, a decision will be taken with regard to whether NN considers this a violation. Subsequently, in case of a violation, a decision will be taken on engagement or restriction.

NN Group will encourage our asset managers to use this paper as guidance to determine risks and opportunities and to engage in a dialogue with companies to address governance risks, that could in our view affect the value of investments. Where needed, we will support these processes with additional tools or guidance materials. This may include more detailed theme or sector policies for areas to be identified of high risk. This paper is developed to help our asset managers in evaluating investments from a governance perspective. By publishing this paper also externally, we aim to express our position and use it to leverage change in the sphere of our investment activities.

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