Guidelines on ESG risk management

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1. Introduction

SpareBank 1 SMN aspires to stimulate a sustainable development of our region. This priority is enshrined in the group strategy for 2020-2023. The group's policy on sustainability will facilitate the attainment of financial goals and create value for our customers, shareholders and employees through being a:

- Driver for the green transition (E)
- Partner for the inclusive development of society (S)
- Guide for responsible business culture (G)

Climate risk is identified as a financial risk at SpareBank 1 SMN. The group's credit strategy sets limits and strategic guides for the lending business, including a long-term ambition to achieve net zero emissions in the group's loan portfolios by 2050. Transition plans at sector level will be drawn up for all significant sectors as part of our effort to help our customers achieve a successful transition.

The credit policy and lending authorisations will accordingly be designed to ensure that ESG risks and greenhouse gas emissions are included as key assessment criteria in the granting of credit and customer follow-up, and lending authorisations will reflect the fact that high ESG risks and greenhouse gas emissions entail increased risk for the bank. The group will make a targeted effort to reduce both ESG risks and greenhouse gas emissions from the loan portfolio.

Green bonds are a source of finance for the group that are competitively priced, attract great demand and contribute to the group's green profile in the financial market. Customer and lending processes shall include an assessment of customers and investments under requirements set in the green bond framework. The group shall over time increase the proportion of loans which can be financed using green bonds.

The purpose of these guidelines is to:

- Contribute to the group's attainment of its financial goals in the long term
- Provide clear guidance to customer advisers in the credit process
- Inspire the group's customers, suppliers and partners to commit to take account of climate and environmental, social and corporate governance issues

2. The bank's corporate social responsibility (ESG – Environmental, Social and Governance factors) in its credit activities

In order to ensure sustainable financial value creation, all granting of credit needs to take into account and support the principles established by the bank's board of directors, including the sustainability strategy, credit strategy and policies and guidelines addressing sustainability. The board of directors has declared an ambition to reach net zero emissions by 2050, illustrating SpareBank 1 SMN's intention to be a driver of the green transition.

In credit cases, the debtor and activities of the debtor with a bearing on ESG will be analysed and described on a par with other possible relevant risk drivers. Such assessments will be assigned significant and, in defined cases, crucial weight in the granting of credit.

Sectors where the bank is involved as a provider of finance pose varying degrees of intrinsic risk. Intrinsic risk will accordingly be a key point of reference for guidelines and policies established by the bank for each sector. The bank also establishes sectoral guidelines on ESG-related risks, in relevant sectors, to ensure that decisions are made on a sound basis and in accordance with the group's sustainability strategy.

3. Credit assessment of customers/loan applications:

ESG factors shall be included as an integral part of the overall credit risk posed by the customer/loan application. The customer adviser shall in the dialogue with customers consider, discuss and bring to light how the customer/borrower handles ESG risks in their corporate governance. The customer adviser shall invariably include assessments with respect to the climate, environment, social issues and corporate governance when processing a loan application. Both the current situation and future situation of the borrower must be included in the assessment.

The bank's credit assessment of a customer/loan application shall address the following:

- Whether activities/purposes/sectors are excluded from financing
- Classify the customer's risk level in relation to ESG using the bank's analysis tools
- Assess the customer and loan application in light of the bank's general and sector-specific guidelines on ESG risks
- Verbally assess the concrete processes and measures applied by the customer to manage ESG risks

4. Risk assessment process for ESG

4.1 Activities and sectors that are excluded from financing

The bank continually reviews activities and sectors that are excluded from financing in light of the bank’s principles for ethics, sustainability, governance and social issues.

In general the production of, and trade in, goods or services that are deemed to be unlawful under a country’s laws and regulations, lists of sanctioned countries/persons or international conventions are excluded from financing and customer relationships at SpareBank 1 SMN.

In addition to the above, the bank defines activities/sectors as excluded from financing based on principles of ethics and sustainability. Borrowers with links to the following sectors or activities are excluded:

Activity/Sector	Excluded
General	Production, trade in, goods or services deemed to be unlawful under a country’s laws and regulations, lists of sanctioned countries/persons or international conventions
War/crises	Companies in need of credit facilities that exploit crises, war situations, dependency or particular vulnerability of individuals or communities. For example through gross overpricing, profiteering from war, conflicts or disasters etc.
Protected areas	Financing of companies that damage natural areas. Financing of protected areas may be granted exemption where licences have been granted by public authorities and in line with rules and regulations.
Seafood/fishery	Financing of unregulated fisheries
Animal welfare	Farming of fur animals
Porn industry	Sector excluded
Tobacco industry	Sector excluded
Arms industry	Companies that produce arms which in normal use violate fundamental human principles. This includes actively dissociating ourselves from cluster munitions and anti-personnel landmines, as well as from companies which develop and produce key components for nuclear weapons, chemical weapons and biological weapons. Companies which export arms shall have in place a policy to ensure that no export of arms takes place to areas where human rights violations are known to occur, or to countries where owing to widespread corruption or civil war there is a large likelihood of arms ending up in such areas.
Child labour and equality/non-discrimination	Companies which fail to respect people’s rights to equal treatment and dignity. This entails not discriminating or differentiating with a basis in age, gender or religion. We also expect a company employing minors to assume responsibility over and above minimum requirements as to prohibition of child labour and to respect children as a vulnerable group with rights under the UN Convention on the Rights of the Child. Employers must also facilitate education. Education is among the most important means for eliminating differences, and access to education is a right of young people.
Mining	A guiding principle in mining is that: 1. encroachments in nature shall be minimised and, regardless of local legislation, plans shall be in place for the purification of emissions and return of areas to their natural status and for repair of environmental harm after closure of a mine

	2. we also require run-off and environmentally hazardous waste to be properly handled, and employees shall have good working conditions that pose low risk to health 3. encroachments in nature must be carried out in such a way that indigenous peoples' rights and opportunities to continue their traditional way of life are not disrupted unnecessarily. A prerequisite is that businesses enter a dialogue with affected parties to find solutions 4. particular caution shall be shown in particularly vulnerable natural environments, and mining operations shall be avoided in areas where accidents or external influences may lead to irreparable damage to the environment 5. We dissociate ourselves from mining operations where entire mountain tops are blasted off, from extraction of uranium and from opencast mining in oil sand / tar sand.
Coal power/coal extraction	Sector excluded
Nuclear power	Sector excluded
Energy source	Companies which utilise controversial energy sources such as nuclear power and coal in their activities
Hydroelectric plant	Hydroelectric plants which fail to comply with the Water Resources Act

4.2 Classification of risk level

Classification of risk level is a requirement applied to all exposures ≥ NOK 10 million. For customers with exposures < NOK 10 million no risk classification requirement applies, but a verbal assessment is required in the case of observed negative discrepancies.

The customer adviser is responsible for classifying risk level, where appropriate in conjunction with the bank's Credit/Analysis Department. The bank's current ESG analysis tool is used for assessment purposes. Where additional information is available, negative or positive, which is not taken into account in the model, this must be described verbally in the processing of the loan application concerned.

4.3 Sector-specific guidelines and transition plans

The bank's credit rules (Credit ABC part B) enshrine specific ESG-related guidelines for the respective sectors. Moreover, work has started on transition plans for the individual sector which will support an organised transition to the net zero goal:

- Property Lease
- Property Project
- Fish farming
- Fishery
- Shipping
- Agriculture (See the document "Sustainable agriculture" under "Transition plans towards net zero")

4.4 Verbal assessment when processing a loan application

Where a loan is to be granted, an assessment shall be made of the customer's management of climate, environmental, social and governance issues in his business. The assessment shall elucidate the customer's current situation and initiated/completed measures, as well as the customer's future measures and plans for the management of ESG risks in his business.

5. Decision-making level

The intention is to define the decision-making level in terms of ESG risk score once satisfactory analysis tools become available. ESG risks will until further notice be assessed at the ordinary level of decision making.

6. Follow-up of customers classified as high ESG risk

Customers classified as high ESG risk are identified each quarter for assessment and inclusion in a watchlist and possible preparation of an action plan.

If reputational risk for the bank is considered particularly high, the board of directors must be informed.

7. Green bonds

The bank has a growth strategy of 10 per cent for customers that qualify for green bond funding. Qualifying criteria:

1. Commercial property
   Construction year as from 2010 (Hotels as from 2011)

2. Fishery
   MSC certification

3. Fishing industry
   MSC, BAP, ASC, Global G.A.P/GGN certification

4. Other
   Hydropower (100%)
   Companies with Eco-Lighthouse certification

Applicants that qualify are given priority provided the applicant's / application's credit risk is satisfactory.