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Sampo Group

Risk Management Principles

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Sampo Group Risk Management Principles

Approved by Sampo plc Board of Directors on 2 November 2022

Scope of application

With these general guidelines, Sampo's Board of Directors confirms the underlying principles regarding risk management within the Sampo Group companies.

Sampo's Board of Directors requires that all activities involving the exposure of any Sampo Group company to risks, as well as all activities controlling those risks, are arranged to comply with these general guidelines and related instructions, especially instructions and policies regarding remuneration provided by the Board, as well as with applicable legislation and regulations. The Board of Directors will supervise the risk taking and risk control activities in a manner deemed appropriate to ensure full compliance.

The principles laid down herein apply to all Sampo Group companies. Sampo plc's subsidiaries' company specific policy and governance documents should follow these principles, taking, however, into account the requirements of different jurisdictions where they operate in and other specific requirements of the business. Company specific policies must cover specifically areas mentioned in Article 44 of Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II directive). In case of conflict between these principles and locally binding set of rules, the locally binding set of rules prevails, and company specific risk management policies shall be aligned with normative requirements.

Paragraphs 3.1, 3.4 and 3.5 in Section 3 ("Risk management organisation") are reflecting subsidiaries' current decisions on risk governance and are not Group level guidelines.

1. The purpose and objectives of risk management

The purpose of risk management is the creation and protection of value. The risk management system is part of the larger internal control system, and it integrates risk management into the governance of the Group and into its significant activities and functions, including decision-making. The risk management system includes the risk management principles given in this document and the corresponding policies, in addition to the organisational structures and processes by which risks are being managed.

For financial sector companies in general, the core competences of business are skilful pricing of **risks inherent in business operations** and proper management of arising risk-exposures and capital needed to cover these risks. High-quality management of these risks is a necessary prerequisite of a going concern, and this document covers the principles for managing them in Sampo Group. Independent risk management functions in each Sampo Group company are responsible for controlling risk management within the company. In addition, Sampo Group Risk Management function controls risk management on the level of the Group.

Good reputation is of paramount importance for companies in the financial sector. **Reputational risk** realises as a loss of confidence in the integrity of the institution among its stakeholders. Since the confidence of our stakeholders towards us is the basis for our long-term profitability, the tools to protect it must be diverse and embedded in the corporate culture. Core values behind the corporate culture are set in Sampo Group's Code of Conduct document that shall be complied with by all Sampo Group employees. Line management in all business areas is responsible for that all their subordinates understand the importance of reputation to Sampo Group, while all employees within the Group are responsible for arranging their work in a way where Sampo Group's reputation is safeguarded. Each Group company's executive management shall ensure that events threatening reputation are always reported in a timely manner to the company's Board of Directors and to the parent company in cases when a realised event might affect the whole Sampo Group.

Business risks have crucial role in the future success of each company. Since there is no capital requirement for business risks and the management of them is primarily the responsibility of the executive level senior management, the business risks have been covered in these risk management principles at general level only.

In Sampo Group, the key objectives of risk management are:

Balance between risks, capital and earnings

- to ensure that risks affecting profitability as well as other material risks are identified, assessed and analysed;
- to ensure that capitalisation is adequate in terms of current risks inherent in business activities and business risks, taking into account the expected profitability of the businesses;
- to ensure that risk-bearing capacity is allocated into different business areas in accordance with the strategy; and
- to ensure that underwriting risks are priced reflecting their inherent risk levels, and that expected returns of investment activities are in balance with their risks and consequential risks are mitigated sufficiently.

Cost efficient and high-quality processes

- to ensure that client service processes, internal operative processes and external reporting are cost efficient and of high quality;
- to ensure that decision-making is based on accurate, adequate and timely information; and
- to ensure continuity of operations and fast and comprehensive recovery in case of discontinuity events.

Strategic and operational flexibility

- to ensure that external risk drivers and potential business risks are identified, and the company is in a good position, in terms of capital structure and management skills, to react to changes in business environment; and
- to ensure that corporate structure, knowledge and processes in companies facilitate effective implementation of changes.

When the above targets are met, risk management is contributing positively on return on equity and mitigating the yearly fluctuations in profitability. Risk management by assuring maintenance of supervisory authorities' and other stakeholders' confidence in Sampo Group is also contributing positively on reputation. Risk management is therefore considered to be one of the contributors in creating value for the shareholders of Sampo plc.

To meet these objectives Sampo's risk management shall include the following prerequisites and tasks.

The central **prerequisites** to be in place for facilitating successful risk management are as follows:

- Risk management governance structure and authorisations (see Section 3, Risk management organisation) and clear division of responsibilities between business lines and independent functions
- Companies' own risk policies and more detailed instructions related to risk management
- Prudent valuation, risk measurement and reporting procedures

The central **tasks** in the risk management process are as follows:

- **Identification of risks:** The risks involved in business operations and business environment, are monitored continuously together with earnings potential. In particular, when new services are launched or business environment is changing, earnings potential and risks including reputational risks shall be thoroughly analysed. Risks, which Sampo Group companies face, are defined in Appendix 1 (Risk definitions).
- **Assessment of capital need:** The capital need to cover measured risks, risk-based capital, is assessed and analysed regularly by risk types and over risks and business areas. In addition, management considers the size of the buffers over risk-based capital to get actual amount of capital. Capital management process is defined in Appendix 2 (Capital and liquidity management).
- **Pricing of risks:** Sound pricing of customer transactions and careful *risk/return* consideration of investments is the prerequisite for achieving the targeted financial performance and profitability over time. In general, starting points of insurance policy

pricing and investment decisions are (i) adequate expected return on allocated capital and (ii) operating costs.

- **Managing risk exposures, capital positions and operative processes:** The risks of insurance liabilities, investment portfolios and operative processes and capital positions are adjusted to maintain a sound risk to return ratio and return on capital (ROC). Management's responsibilities and authorisations are defined on separate documents, e.g. underwriting and investment policies. In addition to internal adjustments of risks and capital, companies can transfer risks to external parties by using derivatives and reinsurance contracts.
- **Measuring and reporting of risks:** Results, risks, profitability and needed capitalisation are measured, analysed and reported by Finance and Risk Management units, which are independent from business activities.

High-quality risk management facilitates the creation of shareholder value for the following reasons:

- **Clients** get a reliable service from a reputable institution and they feel confident when their client relationships are managed in a diligent and prudent manner, with effective risk management;
- Risk premium required by **investors** and **counterparties** will be smaller when risks are transparent and risk management is clearly described and communicated;
- The motivation of the **personnel** strengthens when strategies, authorisations, limits, targeted return and reward criteria are clearly defined and communicated; and
- **Supervisory authorities'** confidence in company's ability to control the risks associated with its activities further bolsters co-operation with the authorities.

2. General Group level risk statements

2.1 Risk appetite and risk strategy

Sampo's risk appetite defines the boundaries for what risk the group is willing to accept in the pursuit of its objectives. It is reflected in Sampo's capital management framework¹ and its risk management strategy.

Risk is an essential and inherent element of Sampo Group's business activities and operating environment. High-quality risk management is a prerequisite for success in all the group's businesses and for assuring a stable result and the delivery of its key financial targets for 2021-2023:

- A Group combined ratio less than 86 per cent
- Progressive insurance dividend
- Solvency II ratio between 170-190 per cent
- Financial leverage less than 30 per cent

Sampo's risk management strategy is to:

- Ensure that risks affecting the profit and loss account and the balance sheet are identified, assessed, managed, monitored and reported in all business activities and at the group level;
- Ensure cost-efficient customer business that is soundly priced in terms of risks and adding value to our clients;
- Ensure the overall efficiency, security and continuity of operations;
- Ensure that risk buffers – in the form of capital and foreseeable profitability – are adequate in relation to the current risks inherent in business activities and existing market environment;
- Limit M&A transactions to bolt-ons in non-life insurance within current markets;
- Dispose non-strategic or otherwise unnecessary balance sheet items and distribute the released capital and reserves to the parent company as appropriate; and
- Arrange its activities in ways that safeguard the Group's reputation, since in addition to the ability to provide value-adding services for its clients and sound capitalisation, the confidence of the clients and other stakeholders is among the most significant assets of Sampo Group.

The link between risk appetite and the risk profile and capitalisation shall be analysed and reported in the risk and solvency assessment² process including analyses of the capital adequacy and regulatory capital requirements under various risk scenarios. Consequently, the process shall influence the Group's strategic risk management and capital management actions.

All Group companies prepare their own risk appetite statements that follow Sampo Group level principles and that are communicated through company-specific policies, which shall include approved risk tolerance limits for the main risk types.

¹ see paragraph 2.2

² ORSA, "Own Risk and Solvency Assessment".

2.2 Risks and capital management

Group level capitalisation is managed within Sampo's capital management framework³, which sets targets for solvency and informs potential risk management actions.

Sampo solvency targets are determined by the Group's ambition to provide an attractive risk-returns profile to shareholders and they reflect Sampo's risk appetite.

- The balance between risks and actual level of capital is analysed and monitored regularly assuming historical circumstances and, from time to time, different stress scenarios defined by the management.
- When a potential imbalance between risks and actual level of capitalisation is identified, the balance will be secured by adjusting existing risk exposures, capital or both. In general, Sampo believes that maintaining the profitability of businesses and active adjustment of risks is the first line of defence in risk management and, in a long run, even more important factor than capitalisation.

Sub-groups and their companies shall monitor the size of their capital buffers and have practices in place to maintain actual amount of capital always over the defined capital floor.

In addition to solvency, Sampo's capital management framework sets targets for debt leverage, which reflect a broad range of criteria including the availability of debt capacity.

- Sampo considers debt capacity as an important source of holding company liquidity and solvency capital in a stress event, and therefore aims to ensure reliable access to debt capital markets.
- Sampo's holding company liquidity reflects the risk that Sampo plc may need cash in periods when access to capital markets could be limited. Key considerations in this regard include debt redemptions and potential shortfalls in subsidiary capitalisation.

2.3 Division of responsibilities

- The Group's holding company, Sampo plc, is responsible for the Group's capital management activities. These actions are guided by targets set for Group level solvency and debt leverage and they include decisions on Group level investment exposures, business growth and performance targets, reinsurance strategies, capital distributions and capital instrument issuances. In addition, Group level risk accumulations and concentrations are (i) prevented by organising the division of responsibilities carefully between the companies, (ii) monitored regularly in Audit Committee, and (iii) managed by adjusting aggregated risks where necessary.
- Group level reporting of financial results and risks are the responsibility of Sampo plc's Group Finance and Risk Management units, which are independent from business operations.
- The subsidiaries' line organisations are in charge of pricing their products and services and organising their sales and implementation processes, for ensuring the profitability, efficiency, quality, security and continuity of their operations as well as the liability towards the clients. They are also responsible for the management of assets and liabilities, risks and capitalisation on the sub-group and company level.

³ For more details, see Appendix 2 Capital and liquidity management

- Most of the risk management activities are performed by the subsidiaries, which are required to organise their risk management activities - identification, assessment, measurement, monitoring and adjustment – within the principles and definitions described in this guideline and within the return and capitalisation targets approved by Sampo plc's Board of Directors.
- Companies can outsource their functions where they deem it efficient, while bearing in mind that core business functions, being critical success factors, shall not, as a main rule, be outsourced outside Sampo Group. If certain activities are outsourced the relevant Sampo Group company nevertheless always carries the ultimate responsibility and risks of the outsourced operation. The Group companies engaged in outsourcing activities shall ensure that they comply with the relevant regulation and authorities' instructions/recommendations regarding outsourcing and are encouraged to maintain an outsourcing policy that shall be complied with in all outsourcing arrangements.
- Companies will decide on company-specific risk policies and their risk reporting to management committees and their Board of Directors independently within their internal governance structure. However, they are also responsible for reporting of risks to the Group CRO, as authorised by Audit Committee, as defined by Group CRO (see section 4).

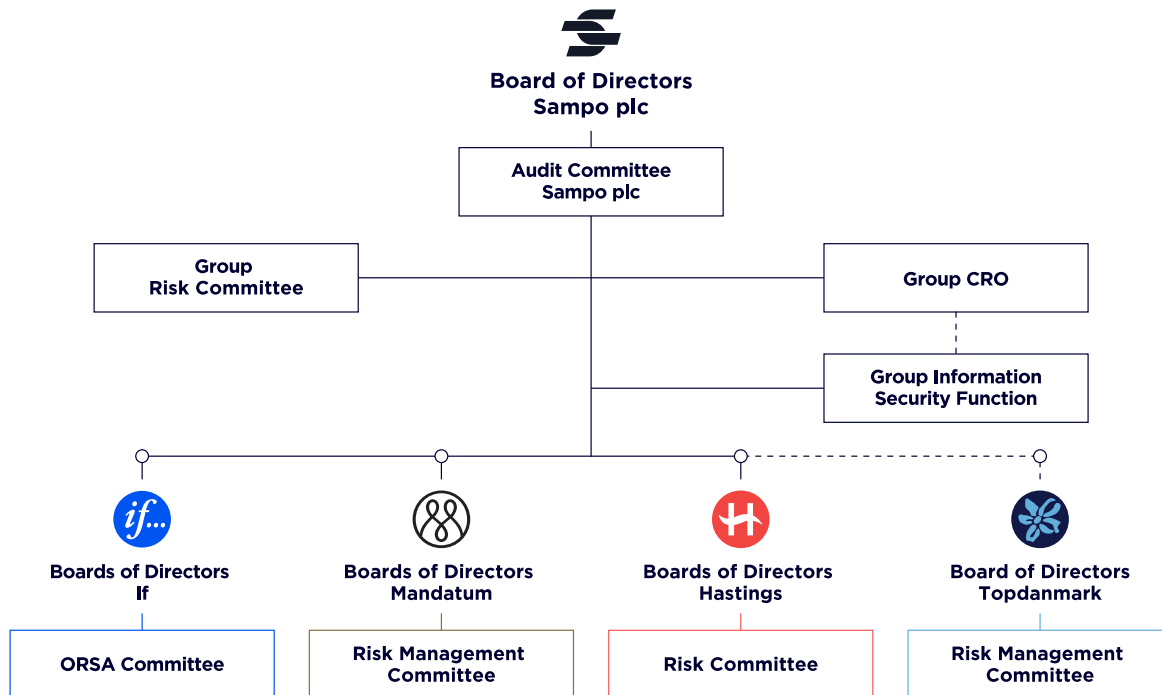
3. Risk management organisation

3.1 Risk management governance framework

Sampo Group companies organise their business activities, internal control and risk management according to group-wide principles of which the most important are Code of Conduct, Internal Control Policy, Risk Management Principles, Remuneration Principles, Compliance Principles and Disclosure and Communication Policy. They approve their own more detailed policies and instructions and organise their reporting to management bodies by themselves.

However, they have also group-wide reporting responsibilities that are, to the extent applicable, both in line with (i) the requirements in European Insurance and Occupational Pensions Authority EIOPA's guidelines for "System of Governance" and (ii) the internal requirements within Sampo Group, as described in section 4. Reporting must take into account the specific features of companies' business activities and their business environment.

Risk management governance framework in Sampo Group



3.2 Sampo plc’s Board of Directors

Sampo plc’s Board of Directors

- makes decisions regarding Group level risk management principles and other general guidelines. Risk management activities and internal control will be organised in accordance with the decisions of the Board of Directors;
- makes decisions on Group strategies;
- makes decisions on overall guidelines regarding capital management and performance targets;
- makes decisions on key monitoring principles; and
- appoints an Audit Committee.

3.3 Audit Committee

Sampo plc’s Board of Directors has established an Audit Committee, of which duties related to risk management and internal control are defined in Audit Committee’s Rules of Procedure as confirmed by Sampo plc’s Board of Directors.

3.4 Subsidiary companies' Boards of Directors

Subsidiary companies' Boards of Directors

- within their decision-making authority, organise the business activities of the subsidiaries to implement strategic decisions made by Sampo plc's Board of Directors;
- make decisions on specific risk-taking policies, capitalisation, risk limits and the delegation of authorisations within the framework provided by approved Sampo guidelines or otherwise binding decisions by Sampo's Board of Directors;
- control risks subject to capital requirements and capitalisation and be in charge of regulatory solvency and internally assessed solvency at all times;
- appoint persons to specific committees (among others underwriting, investment and risk committees, as deemed appropriate) and approve the policies and plans prepared by them;
- make decisions on policies regarding the management of risks and supervise their implementation;
- make decisions regarding the calculation principles for life and non-life insurance products and supervise their implementation;
- make decisions regarding the principles on reinsurance coverage of life and non-life insurance policies and supervise their implementation; and
- must ensure that all critical processes - client services, internal processes and external reporting - have clear ownership that include responsibility to maintain high quality of these processes. Especially information and communication technology (ICT) assets, services and systems, information assets and security as well as the resiliency of operations should be areas of focus.

3.5 Subsidiaries' risk committees

If P&C Insurance Holding's and its subsidiaries' Board of Directors and Mandatum Life's Board of Directors have each appointed separate committees with specified duties and tasks.

In If P&C all risks are monitored in If's Own Risk and Solvency Assessment Committee (ORSA) chaired by If P&C Insurance Holding's Managing Director. The separate risk committees in If P&C reporting to the ORSA are the Actuarial Committee, Underwriting Committee, Reinsurance Committee, Reinsurance Security Committee, Investment Control Committee, Information Security Committee, Ethics Committee, Sustainability Committee, Internal Model Committee and Operational Risk Committee. The Chair of each committee is responsible for organising the required reporting to the ORSA. In addition, there is Compliance Committee reporting directly to If P&C Board of Directors.

In Mandatum Group risks are monitored in Risk Management Committee (RMC) chaired by Mandatum Holding's Group CEO. The separate risk committees reporting to RMC are Asset and Liability Committees, Insurance Risk Committee, Information Security and Cyber Risk Committee and Operational Risk Committee. In addition, in legal and compliance issues, business and reputation risks and business issues regarding the Baltic countries are reported to RMC by responsible line organisations.

The Boards of the Hastings Group's trading entities delegate the oversight of the respective companies' Risk Management Frameworks to the relevant Risk Committees. Each company has its own risk management governance arrangements to ensure all risks are reported to, and reviewed by, the respective company Board and its Risk Committee.

Topdanmark's risks are monitored by the risk management function. It reports to the Risk Committee, which is responsible for risk policies, risk limits, solvency calculation, capital plans, own risk and solvency assessment (ORSA), and partial internal model for non-life insurance risks. The Risk Committee has set up the Model Committee, which is responsible for developing and operating Topdanmark's internal model. The Risk Committee reports and makes recommendations to the Board of Directors via the Executive Board.

Sampo plc's investment activity and related risk management is governed by Sampo plc's Balance Sheet Policy.

3.6 Group Chief Risk Officer

Sampo plc's Risk Management function is organised under the Group Chief Risk Officer (CRO). In addition, the Group Information Security function has an indirect reporting line to the Group CRO. Both of these functions report directly to the Sampo Board of Directors and Audit Committee.

Scope of responsibility:

- Secure a holistic view of the risks Sampo Group is exposed to, including monitoring and measuring Sampo's aggregated risk exposure as appropriate;
- Co-ordinate the risk management work within the Group;
- Co-ordinate and monitor company specific and Group level risk reporting;
- Conduct continuous independent risk analysis based on available risk reporting; and
- Suggest changes in policies, guidelines and instructions related to risk management.

3.7 Group Risk Committee

The Sampo Group Chief Financial Officer (CFO) chairs the Group Risk Committee that ensures communication and cooperation in supporting risk management, including internal control, and risk reporting in Sampo Group. The committee assists both the Board of Directors as well as the Group CEO in the effective operation of the risk management system by:

- Monitoring that all material risks within the Group are assessed, managed, and reported as they should; and
- Monitoring and assessing whether the Group's short-term and long-term aggregate risk profile is aligned with its risk strategy and capital requirements.

Members of the Risk Committee include the Chief Risk Officers of Sampo's wholly owned sub-groups and the Group CRO, who is in charge of presenting any relevant analysis or assessments made in the Risk Committee to the Sampo Board's Audit Committee. The Chair may invite to specific agenda points in the meetings any other persons representing Group companies, including Topdanmark.

4. Risk reporting

4.1 Regular risk reporting

At Group level profits, risks and capital are reported at least quarterly and reporting shall mainly be based on reporting undertaken in sub-groups. In addition to reports covering sub-groups, Group level risk concentrations shall be monitored separately. Also, parent company's capacity to generate liquidity shall be covered in the reporting.

The Group CRO, authorised by Audit Committee, must receive at least quarterly risk reports covering all relevant risks. Regular risk reports provide the Group CRO with aggregate and analysed information about the risks defined in Appendix 1 and these reports are basis for Group level risk analysis prepared for Audit Committee. Group CRO maintains a list of reports to be provided regularly by all Group companies. Group CRO together with Group companies' risk management functions is responsible for continuously developing contents of regular reports.

For more details of risk reporting procedures, see Appendix 4 (Sampo Group's Own Risk and Solvency Assessment ("ORSA") Policy).

4.2 Non-regular risk reporting

In addition to regular risk reports, there are two kind of other risk reports:

1. **Group CRO requests:** Group CRO may ask companies to prepare an analysis/review on subjects that need special attention. The purpose of these reports is to deepen Sampo Group's understanding of the subject in question and the risks related thereto. Based on the report provided, the Group CRO together with the relevant company shall analyse whether there is need for actions to mitigate the possible risks.
2. **Severe incidents:** The purpose of incident reporting procedure is to enable Group management's preparedness for mitigating actions. Additionally, it contributes to ensuring that all employees understand the significance of reputation to all Group companies and the provisions of the Code of Conduct that apply to all Sampo Group employees.

Group companies, based on their established reporting practices, shall inform their Board of Directors on realised risk events and/or identified threats, which may (i) cause significant financial losses directly or indirectly and/or (ii) threaten the reputation of the company, immediately after becoming aware of them. Rapid provision of all then available information is of essence for the Board's capability to contemplate appropriate risk management actions, if any.

If the incident potentially affects the reputation and/or financial standing of the entire Sampo Group and/or Sampo plc, the CRO of the company, or the person nominated by him/her at his/her absence, shall inform immediately also Group IR, Compliance and Risk Management.

Prudent analysis and a report of the incident shall be made without delay after the relevant parties have been informed about it. The CRO of the company, or his/her order, is responsible for delivering the report to their Board of Directors and the Group CRO. The company together with the Group CRO shall then analyse the severity of the event and whether there is a need for reporting to any authority and/or to Sampo Group Audit Committee. If no authority and/or Audit Committee reporting is needed, the event shall be covered in the regular reporting in accordance with section 4.1.

Group CRO also maintains a non-comprehensive list of events causing a reporting obligation to Group IR, Compliance and Risk Management (Appendix 5 (Examples of non-regular reporting)). The specific form of reporting shall be agreed between the relevant organisations.

Appendix 1

Risk definitions

From risk management's perspective, risk in business operations can be defined as the probability of adverse development leading to the result of the operations being worse than expected. When managing the risks, relevant is to be able to identify, quantify and adjust risks so that the negative consequences of risks (i.e. losses or decreased profits) are within toleration limits and that earnings potential justifies chosen risk exposures.

Risks can be classified in many ways. In Sampo Group the risks associated with business activities fall by definition into three main categories: (i) business risks, (ii) reputational risks and (iii) risks inherent in business operations. Within those main categories risks are categorised mainly by underlying risk sources. The (potential) concentration of any particular risk is, as such, not specified as an own risk type.

1. Business risks

Business risk is the risk of losses due to changes in the competitive environment and/or lack of internal operational flexibility.

Unexpected abrupt changes or already identified, but internally neglected trends can cause larger than expected fluctuations in profitability when volumes, margins, costs and capital charges change and in the long run they may also endanger the viability of Sampo Group's business models.

External drivers behind such changes are varied, including for instance general economic development, changes in commonly shared values, developments in the institutional and physical environment and technological innovations. Because external drivers are interconnected, customer preferences and demand can change unpredictably and there may be a need to change regulations as well. In case company's internal understanding of needed changes or willingness and ability to act accordingly is inadequate and competitors are more able to meet clients' and regulation's altered expectations, the company is highly exposed to business risk.

Due to the predominantly external nature of the drivers and development in the competitive environment, managing business risks is the responsibility of the executive level senior management. Proactive strategic decision making is the central tool in managing business risks, which relate to the competitive advantage. The maintenance of internal operational flexibility – i.e. the ability to adjust the business model and cost structure when needed – is also an efficient tool in managing business risks.

Business risks do not have a regulatory capital charge, although they may be a material source of earnings volatility. Because of this, business risk may have an effect on the amount and structure of actual capital base, if deemed prudent in existing business environment.

2. Reputational risk

Reputational risk refers to the risk that adverse publicity regarding the company's business practices or associations, whether accurate or not, causes a loss of confidence in the integrity of the institution.

Reputational risk is often a consequence of a materialised operational or compliance risk and manifests often as a deterioration of reputation amongst customers and other stakeholders. Reputational risk is related to all other activities as well. As the roots of reputational risk are varied, the tools to prevent it must be diverse and embedded in the corporate culture. The corporate culture, which is based on the core values of *business ethics, loyalty, openness* and *entrepreneurship*, is thus seen as an essential tool in preventing reputational risk in Sampo Group. These core values are reflected in how Sampo deals with environmental issues and its core stakeholders in society (i.e. customers, personnel, investors, other cooperation partners, tax and supervisory authorities) and how Sampo Group has organised its corporate governance system.

3. Risks inherent in business operations

The management of risks inherent in business operations – earnings risks and consequential risks are the responsibility of the business areas and investment units in decision-making sense, and at the same time, come under the supervision of independent risk control.

3.1 Earnings risks

In its underwriting and investment operations, Sampo Group is consciously taking certain risks in order to generate earnings. These earnings risks are selected carefully and managed actively. Underwriting risks are priced reflecting their inherent risk levels and the expected return of investments is compared to the related risks. Furthermore, earnings risk exposures are adjusted continuously and their impact on the capital need is assessed regularly.

Successful management of underwriting risks and investment portfolio risks is the main sources of earnings for Sampo Group companies. The day-to-day management of these risks i.e., maintaining them within given limits and authorisations, is the responsibility of the business areas and the investment units.

Non-life underwriting risks

Based on Solvency II regulation, underwriting risk in non-life insurance is often divided in *premium and catastrophe risks* and *reserve risk* in order to distinguish between the risks related to unexpired and expired contracts.

Premium risk relates to future claims resulting from expected insured events which have not occurred on or before the balance sheet date. The frequency, severity and timing of insured events and hence future claims may differ from those expected. As a result, the claims cost for future claims exceeds the expected level and there is a loss in financial accounting or adverse changes in the value of insurance liabilities.

Catastrophe risk can be seen as an extreme case of premium risk. It is the risk of extreme or exceptional events, such as natural catastrophes, where the pricing and setting of provisioning assumptions include significant uncertainty. These events may lead to significant deviations between actual claims and the total expected claims resulting into a loss or adverse changes in the value of insurance liabilities.

Reserve risk relates to incurred claims resulting from insured events which have occurred at or prior to the balance sheet date. The amount, frequency and timing of claim payments may differ

from those originally expected. As a result, technical provisions are not sufficient to cover the cost for already incurred claims and there is a loss or adverse changes in the value of insurance liabilities.

Life underwriting risks

Biometric risks refer to the risk that the company has to pay more mortality, disability or morbidity benefits than expected, or the company has to keep paying pension payments to the pension policy holder for a longer time (longevity risk) than expected at the time of pricing the policies.

In life insurance, catastrophe events include – as in non-life insurance – rare single events, or series of events, usually over a short period of time and, albeit even less frequently, longer lasting events. When a low frequency, high severity event or series of single events lead to a significant deviation in actual benefits and payments from the total expected payments, catastrophe risk, i.e., an extreme case of biometric risk, has realised.

Behaviour risks arise from the uncertainty related to behaviour of the policyholders. The policyholders have the right to cease paying premiums (lapse risk) and may have a possibility to interrupt their policies and withdraw their savings (surrender risk).

Expense risk arises from the fact that the timing and/or the amount of incurred expenses related to management of insurance policies differs from those expected at the timing of pricing. As a result, expense charges originally assumed may not be enough to cover the realised expenses.

Market risks

Market risks refer to fluctuations in the financial results and capital base caused by changes in market values of financial assets and liabilities, as well as by changes in the economic value of insurance liabilities. The changes in market values and economic values are caused by movements in underlying market variables such as interest rates, inflation, foreign exchange rates, credit spreads and share prices.

Furthermore, market risks include also changes in the volatility of market variables, risk of worsening market liquidity in terms of widening bid-ask spreads and the risk of unexpected changes in repayment schedules of assets. In both cases the market value of financial instruments in investment portfolio may change.

Risks and returns in different markets are considered when Sampo Group companies enter into investments or sell investments from investment portfolios. The fundamental distinction between market risks and underwriting risks is that relating to market risks Sampo Group is in most cases a price taker and not a price giver.

Market risks are the other major earnings risk for Sampo Group and good performance in this area is a critical success factor.

The company is exposed to **ALM risk** when changes in different market risk variables (e.g., interest rates, inflation, foreign exchange rates) cause a change in the fair values of investment assets and derivatives that is of different size than the respective change in the economic value of insurance liabilities. It has to be noted that the cash flows of insurance liabilities are modelled estimates and therefore uncertain in relation to both their timing and amount. This uncertainty is central component of ALM risk as well.

On balance-sheet level, ALM risks contribute considerably to economic values, risks and the need for capital. To manage them, Sampo Group companies analyse and monitor ALM risks and ALM exposures actively and the risks are taken into account when designing the limit structures, managing investments within limits and authorisations and developing insurance products.

3.2 Consequential risks

Some risks are indirect repercussions of Sampo's normal business activities. They are one-sided risks, which in principle have no related earnings potential. Accordingly, risk management's objective is to mitigate these risks efficiently rather than actively manage them. The mitigation of consequential risks is the responsibility of the business areas and investment units and the capital need for these risks is measured by independent risk management functions.

Consequential risks can be categorised in three separate groups: (i) counterparty default risk of credit risk; (ii) liquidity risk; and (iii) operational risk.

Credit risk by definition comprises *default*, *spread* and *settlement risks*. *Default risk* refers to losses arising from occurred defaults of contractual counterparties (counterparty risk) or debtors (issuer risk).

In case of counterparty risk, the final loss depends on the positive mark-to-market value of derivatives or reinsurance recoverables at the time of default, the value of collaterals and on the recovery rate in the eventual liquidation of the counterparty.

In case of issuer risk the final loss depends on the investor's holding of the security or deposit at the time of default, mitigated by any potential recovery.

Spread risk refers to losses resulting from changes in credit spreads of debt instruments and credit derivatives. Credit spreads are affected when the market's perception of probabilities of defaults is changing. In most cases, issuer risk has already been fully priced as a higher spread and respectively as a lower market value of security before the event of default has occurred. In essence credit spread is the market price of default risk for issued tradable instruments. Because of these features, spread risk including also debt instrument defaults is categorised in Sampo Group under investment portfolio market risks.

Settlement risk realises when one party will fail to deliver the terms of a contract with another party at the time of settlement. Settlement risk can be the loss associated with default at settlement and any timing differences in settlement between the two parties. Settlement risks are mitigated effectively by centralised settlement and clearing systems used by Sampo Group companies.

Liquidity risk is the risk that Group companies are, due to lack of available liquid funds and/or access to relevant markets, unable to conduct their regular business activities in accordance with the strategy, or in extreme cases, are unable to settle their financial obligations when they fall due.

In Sampo Group liquidity risk deals with potential illiquidity of investments, large claims and unexpected non-renewal of insurance policies. In addition, the availability and cost of refinancing and the offered price for financial derivatives affect the Group companies' ability to carry out normal business activities.

The sources of liquidity risk in Sampo Group are either internal or external by their nature. If the company's rating declines or if the company's solvency otherwise appears jeopardised, its ability

to raise funding, sign reinsurance contracts or enter into financial derivatives at a reasonable price is endangered. Moreover, policyholders may also not be willing to renew their policies. If these risks caused by internal reasons realise simultaneously with general market turmoil making the selling of investment assets and refinancing of debt difficult maintaining adequate liquidity may be challenging.

Sampo Group manages liquidity risk by maintaining both parent company's and subsidiaries' creditworthiness and reputation on appropriate level. Also, diversification of business operations exposed to liquidity risks is sought. In particular, the maturity diversification of expected cash flows generated from different business activities is under constant scrutiny. Since there is no unambiguous technique to quantify the capital need for liquidity risk, it is not directly taken into account in capital need estimates. Consequently, only the interest rate risk part of balance sheet level risks is accounted for in the economic capital framework.

Operational risk refers to the risk of financial and/or reputational loss resulting from inadequate or failed processes or systems, from personnel or from external events. This definition includes legal risk but excludes risks resulting from strategic decisions. The risks may realise for instance as a consequence of

- internal misconduct;
- external misconduct;
- insufficient human resources management;
- insufficiencies in operating policies with regard to customers, products or business activities;
- damage to physical property;
- interruption of activities and system failures; and
- defects in the operating process.

Materialised operational risks can cause immediate negative impact on financial results due to additional costs or loss of earnings. In longer term materialised operational risks can lead to loss of reputation and, eventually, loss of customers, which endangers the company's ability to conduct business activities in accordance with the strategy.

Compliance risk is the risk of legal or regulatory sanctions, material financial losses, or loss of reputation, resulting from a company's failure to comply with laws, regulations and administrative orders applicable to its activities. *Compliance risk* is usually a consequence of internal misconduct and hence it can be seen as a part of operational risk.

The principles of managing operational risks in Sampo Group are presented in Appendix 3 (Management of operational risks) to this guideline.

Appendix 2

Capital and liquidity management

Sampo's capital management framework aims to support value creation by enabling its strategy. Quantitative targets are set for Group solvency and Group debt leverage but other metrics are also steered. Subsidiary balance sheets are calibrated to cover needs for business plans and to provide a stable dividend.

Targets for Group level solvency and leverage

Balance sheet targets have been set to provide a high level of protection against Sampo falling below financial limits. The target levels are intended to encourage active steering of the balance sheet, not automatic actions.

Minimum levels of financial resources are set based on the risks and regulatory as well as rating agency constraints faced by the Group. These minimum levels have been defined as 125 per cent for the Solvency II ratio and 35 per cent for financial leverage⁴. **Buffers** on top of the minimum levels are held to ensure business continuity and dividend security, and to finance bolt-on acquisitions:

- **risk buffer** ensures Sampo remains above regulatory and rating agency risk levels in a severe stress event
- **operating buffer** is smaller than the risk buffer and absorbs normal volatility, without consuming any of the risk buffer.

Solvency and debt leverage are managed towards a **target range** which is considered optimal, considering the requisite minimum levels and the above-mentioned buffers:

- Solvency II ratio between 170-190 per cent
- Financial leverage less than 30 per cent.

The target levels ensure high dividend security but without allowing for excessive buffers. Below target levels Sampo can pay ordinary dividends, but excess capital returns would not be considered. Capital generation is used to enable organic earnings growth and attractive shareholders returns. The Group is able to operate below the targets for some time, e.g., after an acquisition but will gradually steer toward the target range. The aim is for Sampo to not consume any of the risk buffer more than briefly. The target levels are reassessed regularly in order to adjust for any potential changes in the risk profile.

The parent company shall additionally monitor Group level risk concentrations and intra-group transactions which have a direct impact on the desired level of capitalisation.

Sub-group capitalization

In Sampo Group's business entities at sub-group and company level, the total need for capital (i.e., the actual amount of capital) is assessed regularly in two-step process as follows.

⁴ Financial leverage calculated as financial debt/(financial debt + IFRS equity)

Defining the capital floor

Capital floor is the minimum level of own funds the company needs to run its business operations normally. The amount of capital floor is the highest of the following three quantitative capital concepts:

- a. Solvency Capital requirement by regulatory Standard Formula;
- b. Solvency Capital requirement by the internal model utilised by the company; and
- c. Rating Agency Capital, i.e., the capital needed to secure the target rating for the company.

When the company is using their own internal model(s), the procedures shall be thoroughly validated and verified, and model approved by its Board of Directors.

Defining the size of the buffer

Because risk exposures and profits evolve continuously over time and capital can sometimes erode rapidly due to stressed situations, there is a need to have a certain **buffer**, which together with the capital floor, as determined by the company in accordance with the above rule, form the actual amount of capital. An adequate buffer gives time for the company to adjust its risks and capital in a controlled manner in times of stress, i.e., at all times maintain the balance between risks and capital. An adequate buffer also gives comfort to supervisors, clients, investors and counterparties of the company's reliability. The following factors are most material when the size of buffer is considered:

- Expected profits – the higher the level of expected profits and the lower their volatility, the smaller the buffer that is needed;
- Business growth prospects - if business is growing, the buffer is larger than in the case of a run-off business;
- Other sources of capital – the more capacity and ability to issue Solvency II compliant capital instruments means that a lower buffer is needed; and
- Uncertainty of measured SCR or other relevant capital requirement – the bigger the uncertainty around the relevant capital requirement's ability to predict future capital needs, the bigger the buffer.

Holding company liquidity

The parent company Sampo plc shall ensure sufficient liquidity to prevent any cash flow pressures. Sampo plc needs liquidity to manage the Group's financing needs, ensure dividend security and to finance potential transactions. Sampo plc funding is limited to internal dividends/investment returns but can periodically be complemented with new capital or asset sales. Hence, holding company liquidity needs to be managed holistically together with the dividend policy, strategic ambitions and balance sheet targets.

Appendix 3

Management of operational risks

The goals of operational risk management are:

- to ensure simultaneously the efficiency and quality of operations;
- to ensure that operations are compliant with laws and regulations;
- to ensure the continuity of business operations in exceptional circumstances; and
- to ensure the ability to recover normal operations swiftly in case of disruptions.

Each company is **responsible** for arranging its operational risk management to align with above goals, taking also into account the specific features of its business activities.

The central **tools** in operational risk management are (i) the identification of risks, (ii) proper preventive actions at all levels of operations, (iii) analysing operational risk events, and (iv) continuity, response and recovery planning. To ensure the use of these tools, **responsibilities** in the following areas must be set clearly:

- drafting and enforcement of adequate operational risk and continuity policies;
- legal and financial compliance of operations;
- continuous development of human resources (knowledge and skills) and work processes;
- day-to-day management; and
- reporting and controlling.

Examples of areas where operational risk management is considered especially important are:

- **Personnel.** To perform their duties with skill and competence, personnel must have adequate experience for their work, as well as the required special skills and training. Also, responsibilities and objectives of employees have to be clearly set, described and adequately communicated.
- **Services, products and information assets.** Risks related to services and products offered as well as information assets owned by or within the custody of the company should be identified to ensure the functionality of the sales, implementation and reporting processes. Risk identification is crucial when new businesses are launched or there are fundamental changes in the way business is conducted.
- **Work processes.**
 - Work processes and user rights to IT systems have to be arranged in such a way that various parts of a process cannot be controlled by one person alone. The duties of individual employees must be organised and segregated accordingly. Moreover, the personnel should have user rights only to data and ICT systems they need for their duties.
 - All information entered into data systems (either related to contractual / customer information or any other relevant information) must be sufficient in scope and accuracy. The accuracy of the information has to be verified using controlling methods appropriate for the business area in question.

- The calculation routines used both in internal (quantifying business development, performance and risks) and external reporting (all client and other stakeholder related reporting) must be verified and documented.
- **Security of information and communication technology.** It must be ensured that information and communication technology security is sufficient and up to date.
- **Physical Property.** Physical security measures (e.g., protection against power failure, fire, water and unauthorised physical access) should be defined, documented and implemented to protect the premises, data centres and sensitive areas from unauthorised access and from environmental hazards.

Appendix 4

Sampo Group's Own Risk and Solvency Assessment ("ORSA") Policy

Background and basis

Once in a calendar year – or more frequently, if required – Sampo Group produces a document covering its own risk and solvency assessment for the Group ("Group ORSA").

This policy defines the general principles, processes and methods used when preparing the Group ORSA. The document aims at producing a forward-looking view on the risks which Sampo Group is exposed to. It also represents Sampo's own view of its risk profile, and the capital and other means needed to address those risks. The Group ORSA document shall include an assessment of Sampo Group as a whole and cover the material risks arising from all the entities that are part of the Group.

The risks associated with Topdanmark A/S are based on the latest available information at the time of the assessment.

The legal framework for the Group ORSA is the set of insurance company regulations and guidelines based on the Solvency II Directive. The Group ORSA is an integral part of Sampo Group's risk management system.

Processes and procedures

As a basic principle the Group level solvency ratios shall be forecasted based on the sub-groups' and associated companies'⁵ risk and capital forecasts on a consolidated basis. Accordingly, the forecasts of each sub-group must be based on common Group level scenarios given by the parent company.

The Group ORSA shall include also analysis of Group level risks, such as risk concentrations, intra-group transactions and profit correlations between different lines of business lines. Also, the liquidity generation capacity – especially at the parent company level – shall be analysed taking into account liquidity buffers and leverage.

Sampo's sub-groups are responsible for preparing their own analysis at sub-group and operating company levels, including solo ORSAs for all individual insurance companies, as required by Solvency II. In case of operating companies with minor significance within the sub-groups, separate analysis is not needed. However, the risks of such companies shall be taken into account in the Group ORSA e.g., as an equity investment when parent company's risks are considered.

The sub-groups must take into account the general guidance and scenarios given by the parent company and the specific features of their businesses.

⁵ Associated companies' numbers are based on latest available public information at the time of the assessment.

Sampo plc as the ultimate parent company is responsible for preparing Group level solvency forecasts. These forecasts shall be based on detailed forecasts prepared by the sub-groups. Forecasts for the associated companies shall be prepared by the parent company⁵. The parent company is also responsible for the risk analysis of group-encompassing issues.

Frequency

The quantitative part of the Group ORSA will be performed annually per Q3 based on the uniform group-wide scenarios in parallel with the financial planning process of the subsidiaries and shall be updated quarterly. The quantitative part of the ORSA shall, where appropriate, also include sensitivity analyses and a reverse stress test.

Because profitability, risks and capital are assessed and monitored quarterly as a part of regular management reporting, these results of the quarterly assessments shall also be utilised in the annual Group ORSA document.

Limits and solvency needs

When the Sampo Group solvency ratio breaches the internal monitoring level set in the latest Group ORSA, that breach shall trigger the need for a Group ORSA outside the regular timescales.

When solvency ratios for sub-groups and/or individual operating companies breaches the internal monitoring level set by the respective Board of Directors for the sub-group and each relevant operating company, such breach triggers the need for an extraordinary update of the relevant sub-group or company level contribution to Sampo Group ORSA. Sampo plc will then evaluate the impact of the update and consider the need for an extraordinary Group ORSA.

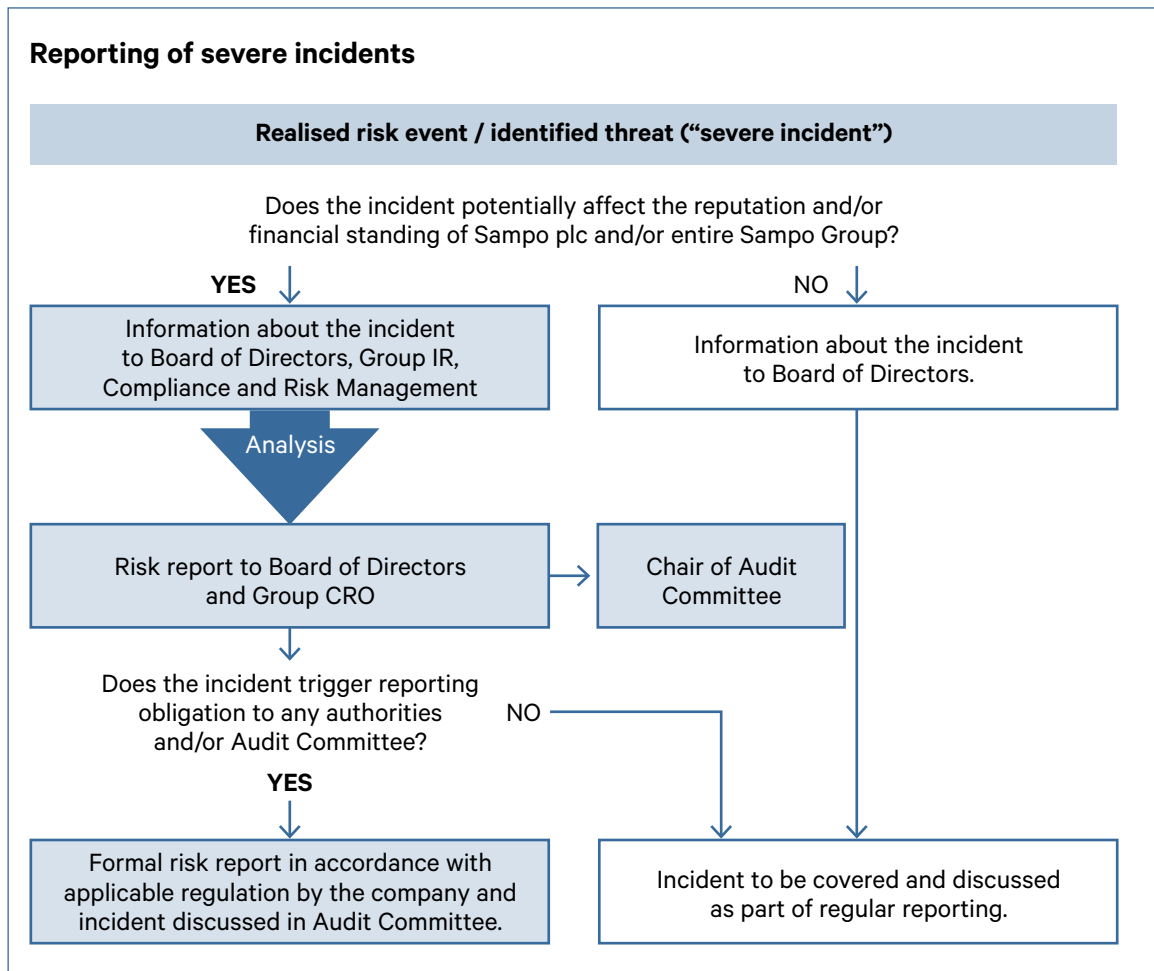
Risk profiles, risk limits and data quality standards

As there are no business operations at Sampo plc other than capital structure and liquidity management and the sub-groups conduct their businesses and risk management functions independently, underwriting and investment risk profiles are assessed and risk limits set mainly in the sub-groups' risk management policies, which are based on the common risk management principles set by Sampo plc. Also, data quality standards are defined at the sub-group level. In addition to monitoring sub-group and solo capitalisation, Sampo plc manages Group level capitalisation within Sampo's capital management framework, which sets targets for solvency and informs potential risk management actions.

Appendix 5

Examples of non-regular reporting


- IT risk within or relating to a critical application or system realised or threatening client service, and/or internal and external reporting processes;
- Critical data security incident;
- Mis-selling;
- Critical failure in reporting obligations to supervisory authorities, for example due to negligence;
- Leak of insider information to any third party as regulated in the Market Abuse Regulation (“MAR”);
- Anti-money laundering issues;
- Group level reputational risk pursuant to a conflict with collectively shared values in the society;
- Other risks or risk events which are relevant on Sampo Group level or critical on a sub-group level





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