KEVA

ANNUAL REPORT 2016

Annual Report 2016

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CEO's review

The year 2016 brought about major changes in Keva's operating environment. Over the course of the year Prime Minister Juha Sipilä's Government made several major restructuring decisions, the most significant of these having to do with the health and social services reform of 2019. If the reforms are implemented as proposed, Keva is becoming expressly a pension provider for municipal and county corporations. The draft Government proposal on legislation to govern health and social services and regional government sets out from the premise that the new actors in health and social services would be member organisations of Keva and that the companies in the county corporations could apply to become Keva's member organisations in the same manner as companies under local government control. The proposed solution is a natural one and serves to safeguard not only the additional pension coverage of transferring personnel but also the funding of pensions. In this context, the decision was also made to re-design Keva' pension contribution structure to match the new structure and financing in local and regional government.

On 5 April 2016, the Government made a decision on including freedom of choice for customers in the health and social services reform. The draft legislation was made public just before Christmas. According to preliminary estimates, freedom of choice would extend to services accounting for roughly one quarter of operating costs in the years 2019–2020 and, as of the year 2023, approximately 40% at least. More detailed estimates will become available at a later date. In Keva's estimation, the personnel payroll breakdown is likely to be very similar.

The number of persons covered by Keva's pension system may nonetheless decline considerably if the customers' freedom of choice integrated into the reform brings about significant changes in the market shares of privately and publicly provided services.

A working group of officials was appointed in December 2016 to temper the impacts of the health, social services and regional government reform on pension systems. The working group is expected to submit its report in spring 2017. Its mandate is to prepare a proposal that allows employees in the sector of health and social services to remain within the same pension system under which they are covered at the end of 2018 irrespective of any change in employer. The decisions on the transitional phase are vital to Keva. If no effective individual solution is in place, there is the risk of upward pressure in equalisation payments, which impacts on local government finances and the financing of the counties. The funding of pensions in Keva's pension system is on a sustainable basis only if there is no foreseeable moment, under current rules, that the estimated pension expenditure could not be funded.

The ministerial working group on health, social services and regional government reform announced in December 2016 the appointment of a working group in spring 2017 to investigate the potential of integrating the local government and private sector pension system and also any other changes to the pension system possibly arising from the health, social services and regional government reform. Keva stands in favour of such a working group. Clear but not excessively narrow boundaries should be set for its terms of reference so as to allow the working group to seek out alternatives that are effective and viable in terms of the insured, employers, the earnings-related pension system as a whole, and public finances alike. The report of the working group will likely provide the foundation for continued consideration of the matter into the next parliamentary term.

Local government finances and personnel

The year in local government saw fiscal adjustments and the pursuit of sustained savings. Analysis of the 2016 financial statements of municipalities and joint municipal authorities indicates that while local government finances have grown clearly stronger on the year, improvements in the efficiency of operations are still being sought. Local government operating costs rose only moderately, by just over 1%, whereas operating income remained unchanged from the year before. Annual contribution margins were boosted by a total of 500 million euro in 2016. Interest-bearing liabilities continued to increase but at a slower rate than before.

According to calculations prepared by the Ministry of Finance, in 2017 the Competitiveness Pact will bring down operating costs in the local government sector by 683 million from 2016. The net impact on local government finances in 2017 will come to -168 million euro, primarily on account of tax revenue losses due to the cut in holiday bonuses and changes in central government transfers to local government.

A survey conducted by Local Government Employers KT shows that savings averaging 1.7% were made in local government personnel costs in 2016. This comes to approximately 350 million euro out of the total local government labour costs of 21 billion euro. Austerity measures in 2017 are estimated to be roughly of the same magnitude as in the previous year. In the near future, local government personnel will mainly be reduced through attrition. Replacement hires are unlikely to match the rate of retirement. According to the KT survey, local government personnel figures will decline in the near future such that in 2018, the sector is estimated to employ 414,000 persons.

The number of persons insured under the local government pension system stood at roughly 520,000 at the end of 2016. This was 2,000 fewer than the year before. Keva's member organisations' payroll under the Local Government Pensions Act was 16,888 million euro, 68 million euro (0.4%) higher than in 2015. Real payroll growth in 2016 was virtually nil. Considerable uncertainty attaches to the development of the payroll in Keva's pension system also in the coming years, especially owing to the freedom of choice aspect in health and social services provision.

Earnings-related pension contributions

The Competitiveness Pact negotiated by the social partners in 2016 was a major achievement in terms of the long-term competitiveness of Finnish labour and Finnish businesses, although it remains to be seen whether the new bargaining system, the 'Finnish model', will be put into practice.

Under the Pact, the employee's earnings-related pension contribution will rise in increments by a total of 1.2 percentage units in the years 2017–2020. The employer's contribution will decline by a corresponding amount. In Keva's pension system, the employee's pension contribution is the same as in the private sector but the employer's contribution is decided by Keva's Council, which decided to reduce the contribution in 2017 by approximately 1.26 percentage units. The 0.86 percentage-unit reduction in contribution levels due to the pension reform of 2017 is accounted for in full in this reduction, which will reduce local government operating costs by approximately 260 million euro.

The year in investments

The year in investments was marked by volatility. The first quarter turned out worse than projected for both the global economy and the capital markets. At the start of the year, the global economy and economic development in the

United States in particular was expected to follow a moderate growth track. Interest rates had fallen to the unimaginably low levels of 2015 and central banks had pumped such massive liquidity into the market that the old playbook truly was becoming outdated.

The positive news about the economy in the second quarter came primarily from the United States, and even there it was more of a ‘good news/bad news’ scenario. Europe continued to wait on economic growth. China was faring rather well and stayed out of the news. The shocker of the quarter was the UK referendum turning in favour of Brexit. Capital market operators, like certainly many others as well, were expecting the vote to come down for staying in the EU. As it turned out, the markets were in for a rude awakening. Once the initial shock wore off, however, higher-risk investments bounced back at remarkable speed, with equities leading the charge.

The third quarter brought about more of the same. Global economic development remained tenuous. Massive stimuli and liquidity had failed to kick-start growth and inflationary development as desired. Regardless, stock markets even for listed securities climbed well into the black by the end of the quarter. Keva’s fixed-income portfolio, for instance, was returning close to 6% by the end of September. Returns were indeed disproportionate to the real world and the real economy and were instead increasingly reflective of the exceptional circumstances in the world economy and the capital markets.

The US election was virtually a replay of the UK referendum in that the outcome left pundits and markets equally surprised. Conventional wisdom had it that a Trump presidency would instil near panic in the markets. As it turned out, a market upswing followed after only a brief slump in the equities market.

The undercurrent in the global economy is now somewhat more favourable than before. The US has strong economic growth and positive employment figures. China is more or less running on an established track as growth declines, and the nation is faced with increasing challenges presented by its demographic changes. Cautious optimism is warranted also with regard to economic growth in Europe, Finland included.

Reforms at Keva

In 2016, Keva continued to gear up for the pension reform taking place in 2017. Tools employed included information system modifications and training provision. A reorganisation was also put into place to strengthen the customer relationships function and communications. The composition of the management group was moreover reviewed. All changes took effect at the start of 2017.

The Keva Act was amended during the year under review in relation to the regional government reform, to expand the scope of organisational membership, and with regard to criteria for charges. Work on drafting provisions for the Keva Act to govern Keva’s administration and the relative powers of its various bodies was also started.

Keva got off to a flying start in 2016 on preparing for what may be the biggest change in its history. Strategic projects have been put in motion to enact reform at Keva by 2019. The aim for 2019 is for Keva to lead the earnings-related pension sector in terms of competitiveness and experience with customers. This ambitious aim can be achieved through a consistent rollout of customer orientation throughout the organisation. This will allow us to provide customer service in keeping with our strategy, service principles and service models. Competitive services and payment policies of high standard will ensure that limited liability companies remain loyal to Keva. Service quality and cost efficiency, already at a good level, will be further boosted by leveraging digital services in particular. Other areas of enhancement include our social responsibility programme and our workplace culture and management.

Keva also provides pension coverage for employees of the State, the Evangelical Lutheran Church, and the Social Insurance Institution of Finland Kela. It has been our experience that the anticipated cost savings have been achieved and that the insured are happy with the service provided.

In 2016, Keva paid out State pensions in the amount of 4,502 million euro, an increase of some 62 million euro or just over 1% from the year before. At year-end, roughly 259,000 State pensions were being paid, just under 2% less than in 2015. Keva also paid out Evangelical Lutheran Church pensions in the amount of approximately 188 million euro, which was 4% higher than in 2015. Keva engages in active cooperation with the State, the Church and Kela alike.

March 2017

Timo Kietäväinen
CEO

Report of the Board of Directors 2016

OPERATING ENVIRONMENT

In 2016, the most intense civic debate in Finland centred on the Competitiveness Pact, the health, social services and regional government reform, and the associated freedom of choice. The measures proposed by the Government aim to improve Finland's finances in both the short and long term. It is especially the freedom of choice for customers envisioned as part of the health, social services and regional government reform that would have the greatest impacts on the pension system of Keva's member organisations.

The global economy experienced exceptional uncertainty in 2016. The UK referendum on leaving the EU resulted in a Brexit victory and the prospect of drawn-out negotiations on the terms of the exit, which are certain to put a damper on economic growth. The outcome of the US presidential election only further contributed to the unsteady outlook for the global economy.

The global economy serves to undermine the outlook for Finland's economy. Positive news were nonetheless forthcoming towards the end of the year: rising confidence in the economy and an end to the long-running recession. The rise in confidence is partly attributable to the favourable development of the rate of employment and unemployment despite long-term unemployment continuing to grow. The downward trend in manufacturing also appears to have been reversed, as the Competitiveness Pact is set to improve price competitiveness in the longer term while monetary policy supports growth. The economy is back on a growth track underpinned by private consumption and investments. Total exports were on the rise, driven by Eurozone exports. Public debt continued to rise and is projected to reach roughly 66% of GDP.

While local government finances are currently fairly stable, the outlook is challenging owing to lacklustre economic growth, a rising dependency ratio and adjustment measures in the public sector. Cost-cutting measures extending also to local government personnel resulted in the payroll in the pension system of Keva's member organisations increasing only very modestly. Municipalities continued their wholesale outsourcing of social and healthcare services to private providers and the topic is certain to come under consideration in many more municipalities.

The health, social services and regional government reform will likely result in over half of the workforce of municipalities and joint municipal authorities transferring into the employ of county corporations at the start of 2019. Certain regional administration duties and the relevant staff will also be transferred from the State to the counties. Under the Government's outlines, the counties will be member organisations of Keva and the companies held by the counties may become member organisations of Keva on the same terms as companies held by municipalities.

An unexpected turn was seen in the health and social services reform in April when the Government specified its position on the freedom of choice for customers. The draft proposal on the reform, freedom of choice excluded, was circulated for comments in the autumn but the details regarding freedom of choice were not made public until December and these were circulated for comments in February. The policy choices would provide for a broad freedom of choice covering activities that give rise to nearly two thirds of all health and social services expenditure.

Freedom of choice will have a significant impact on the numbers of insured in the pension systems and the funding of the systems. In December the ministerial working group on the reforms outlined a transitional approach to mitigate the effects in the years 2019–2025. As a rule, the pension coverage of social and healthcare services employees would be organised in the same pension system as at the end of 2018 for the duration of the transition period.

The year 2016 brought about many surprises, and investment operations were no exception. Little in the way of returns was expected at the start of the year. Interest rates were at historical lows to begin with while the equities market had had a good run of several years since the financial crisis. Despite expectations, interest rates continued to fall and fixed-income investments delivered a return that exceeded all expectations. Equity investments also performed well especially thanks to the rising market towards the very end of the year. In spite of all challenges in the operating environment, 2016 turned out to be a good year in investments.

Keva must evolve in step with its operating environment. The required reforms were organised into Keva 2019 projects, which aim to improve customer relationships, the contribution structure, social responsibility, Keva's brand and corporate culture. Keva will also build on its digital solutions. The management group serves as the steering group for the projects which will be continued in the years 2017–2019.

Changes in legislation

Amendments to pension legislation adopted in 2016

Amendments relating to the pension reform were made in 2016 to the Acts governing public sector pensions and these amendments for the most part enter into force at the start of 2017. Certain technical amendments to clarify enforcement were furthermore made to the pension Acts and the Keva Act.

Amendments made to the Acts governing public sector pensions involved e.g. ones necessitated by the enactment of the new Communicable Diseases Act Provisions relating to protected supplementary pension arrangements in the private sector were complemented with regard to pensioners and persons of retirement age. Those covered by the legislation are entitled to receive public sector pension at the age of 63 without any reduction for early retirement.

Provisions concerning periods of limitation applicable to pension contributions were harmonised to make the same periods of limitation apply to the charging of pension contribution and the refund of unduly paid pension contributions.

Changes in pension contributions relating to the Competitiveness Pact

The Competitiveness Pact resulted in the adoption of amendments to the provisions governing pension contributions. These amendments will cause the employee's contribution to increase and the employer's contribution to decrease in the same proportion. The employee's pension contribution will be increased and the employer's pension contribution decreased by a total of 1.2 percentage units in the years 2017–2020. The employee's pension contribution will be raised by 0.2 percentage units in the years 2017 and 2018 and by 0.4 percentage units in the years 2019 and 2020.

CUSTOMER RELATIONSIPS AND CUSTOMERS

At 31 December 2016, Keva had 2,293 employer customers: 1,033 local government organisations, 968 State organisations and 291 parishes or parish unions. Kela, the Social Security Institution of Finland, is also an employer customer of Keva.

Keva manages the earnings-related pension services of roughly 1.2 million public sector employees and pensioners: approximately 670,000 insured persons and 577,000 pension recipients.

Keva's customer managers had around 300 meetings with customers during the year. In addition, management held 26 partnership road shows to showcase Keva's new account management model for employer customers.

During the year, Keva fielded 152,000 calls from employee customers and nearly 4,000 calls from employer customer representatives. Calls from employee customers increased by 12,300 on the year. General pension advice was sought in 121,800 of the calls from employee customers while the rest concerned payment of pension. Keva sent out 16,550 replies to written enquiries from employee customers in 2016, an increase of roughly 2,200 from the previous year. Customers served by Keva's pension advisory service numbered 885. Since the start of 2016, the customer service desk operated by appointment only. In many cases, the business of customers calling in to make an appointment could be handled already during the initial call.

Keva switched over to a more informal mode of address in its customer letters in 2016. Adjustments were also made to increase the comprehensibility of customer texts, clarify terminology and restructure correspondence for greater customer-friendliness.

Employee customers are embracing the online service to an increasing extent. In 2016 the online service My Pension had 606,000 logins, an increase of roughly 50% on the year.

New calculators catering for the pension reform were introduced in the My Pension service and the application service was upgraded to automatically retrieve the applicant's basic information, which facilitates the process of applying for pension. The upgrades delivered increased customer satisfaction in the online service.

The popularity of online service was also reflected in the number of visitors to Keva's website, which in 2016 had 1.5 million visits, 9% more than in 2015. The employers' online service had 40,471 logins in 2016.

Keva's website and the employers' online service were modernised in 2016 and the new sites were launched at the start of 2017 simultaneously with the unveiling of Keva's new corporate identity.

A new process for the systematic and ongoing collection of customer feedback was created in 2016 and deployed at the start of 2017 as part of the newly launched Keva website.

According to the customer satisfaction survey, 80% of employer customers rates Keva's performance of its duties as good or very good. The equivalent figure among employee customers was 86%.

Employer customers thought that their working relationship with Keva had for the most part evolved in a good or very good direction, with 84% of respondents giving Keva a rating of very good or good on its main service principles of professionalism, delivery on promises, clarity and effortlessness.

Keva's services were perceived as good for the most part and they were judged to have improved over the past year. Customers were particularly satisfied with customer advisory services, which left customers with a favourable and positive impression. Keva is perceived as a prompt, relevant, knowledgeable, friendly and reliable provider of pension services. The pension application process is smooth, clear and easily understood. Customer feedback indicates room for development mainly in isolated customer interactions.

CONTRIBUTION INCOME

At the end of 2016, some 520,000 employees were insured under the local government pension system, i.e. around 2,000 fewer than the year before. The total payroll for employees insured under the Local Government Pensions Act (KuEL) was EUR 16,888 million, which was EUR 68 million (0.4%) more than in 2015.

Local government contribution income in 2016 totalled EUR 4,966 million or 29.40% of the payroll (EUR 5,013 million and 29.81% in 2015, respectively). Contribution income decreased by EUR 47 million (-0.9%) from the previous year. The local government contribution income is made up of four parts: the employer's and employee's pay-based contributions as well as employer's contributions based on pension expenditure and early retirement pension expenditure.

Pay-based contributions were collected in the amount of EUR 3,933 million. The figure was virtually unchanged from the previous year. The employees' share of the contribution was EUR 1,045 million and the employers' share EUR 2,888 million. In 2016, the pay-based contribution was on average 23.29% of payroll, i.e. 0.1 percentage units less than in 2015. The contribution broke down such in 2016 that employees under the age of 53 were charged 5.7%, employees 53 and over 7.20% and employers 17.10%.

In accordance with the decision of Keva's Council, Keva charged EUR 880 million in pension expenditure-based contributions to its member organisations, which was equivalent to 5.21% of the payroll, a decrease of EUR 66 million of 7% from the previous year.

In accordance with the decision of the Council, Keva charged EUR 152 million in early retirement pension expenditure-based contributions, which was 0.9% of the payroll. The sum increased by EUR 18 million on the year.

Financial support is a benefit equivalent to group life insurance paid to the beneficiaries of a deceased local government officeholder or employee. At the end of 2016, 710 member organisations had arranged for financial support through Keva. Keva collected roughly EUR 5.5 million in financial support contributions in 2016, i.e. about EUR 0.6 million less than in the previous year.

Keva received some EUR 185 million in contribution income from the Unemployment Insurance Fund, which was approximately 39 million less than in 2015.

Under law, Keva is also responsible for the calculation and collection of State pension contributions. Keva collects the contributions directly in the State Pension Fund's bank account but is responsible for all related practical measures. In 2016, State pension contributions amounted to just under EUR 1.7 billion. State pension contributions do not impact Keva's profit and loss account.

Local government (KuEL) contribution rates 2007–2016

Year	Employer's contribution rate				Employee's pension contribution rate	Average total
	Pay-based contribution	Pension expenditure-based contribution	Early retirement expenditure-based contribution	Total		
2016	17.10	5.21	0.90	23.21	6.19 [1)]	29.40
2015	17.20	5.62	0.80	23.62	6.19 [2)]	29.81
2014	16.85	6.03	0.91	23.79	6.03 [3)]	29.82
2013	16.45	6.64	0.91	24.00	5.58 [4)]	29.58
2012	16.35	6.21	0.99	23.55	5.57 [5)]	29.12
2011	16.10	6.45	1.00	23.55	5.10 [6)]	28.65
2010	15.60	6.66	1.29	23.55	4.87 [7)]	28.42
2009	15.90	6.60	1.10	23.60	4.62 [8)]	28.22
2008	16.00	6.62	1.08	23.70	4.42 [9)]	28.12
2007	16.50	6.54	0.79	23.83	4.61 [10)]	28.44

[1)] 5.70% for people under 53 and 7.20% for people 53 or over
[2)] 5.70% for people under 53 and 7.20% for people 53 or over
[3)] 5.55% for people under 53 and 7.05% for people 53 or over
[4)] 5.15% for people under 53 and 6.50% for people 53 or over
[5)] 5.15% for people under 53 and 6.50% for people 53 or over
[6)] 4.70% for people under 53 and 6.00% for people 53 or over
[7)] 4.50% for people under 53 and 5.70% for people 53 or over
[8)] 4.30% for people under 53 and 5.40% for people 53 or over
[9)] 4.10% for people under 53 and 5.20% for people 53 or over
[10)] 4.30% for people under 53 and 5.40% for people 53 or over

PENSIONS AND BENEFITS

Keva achieved the strategic targets set for old-age and disability pension application processing times and for service level. These targets measure the continuity of income. Keva was also able further to enhance the quality and comprehensibility of pension decisions. Customer satisfaction among the insured exceeded the target level.

In 2016, Keva implemented major information system changes that had to do with the pension reform taking effect at the start of 2017, and also prepared for the implementation of the reform. Pension decision formats were also adjusted and a less formal mode of address was adopted.

Applications received and decisions issued

In 2016, Keva issued 67,204 decisions, of which 60,056 concerned pension matters, 6,787 rehabilitation and the rest benefits such as financial support, etc. Of the 69,891 applications received by Keva, 62,701 concerned pension matters.

The figures include all decisions on applications received based on the Local Government Pensions Act (KuEL), State Employees' Pensions Act (VaEL), the Evangelical-Lutheran Church Pensions Act (KiEL), and the Social Security Institution Pensions Act (KelaL) pertaining to Kela's salaried employees. Detailed charts by type of pension Act are provided in the Appendix at the end of the report.

The highest number of decisions by far concerned the Local Government Pensions Act: 51,652 decisions or 76.9% of all decisions issued by Keva. State Employees Pensions Act decisions numbered 13,177, Church Pensions Act decisions 1,829 and Kela Pensions Act decisions 546.

Keva shortened its processing times with regard to applications for old-age pension and rehabilitation, whereas the processing times for part-time, survivors' and disability pensions grew longer.

The discontinuation of part-time pension resulted in as many as 39% of applicants wishing their pension to start at the last possible date, 1 January 2017. Details of each applicant's earnings in 2016 were required in order to decide these applications, which contributed to the longer processing times.

A review of the records concerning survivors' pension and disability pension uncovered a few dozen applications which another pension provider should long ago have submitted to Keva. Other delays in the submission of applications also served to lengthen overall processing times.

Decisions issued on time as provided in the service level indicator accounted for 93.1% of all decisions (93.5% in 2015).

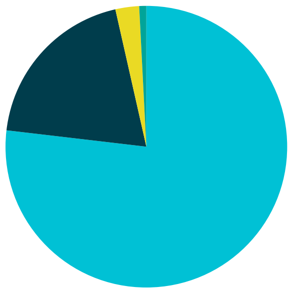
The shortest processing time was achieved in respect of rehabilitation applications, on which a decision was issued in an average of 12 days. The average processing time for survivors' pensions was 18 days, old-age pensions 20 days and part-time pensions 27 days. The longest processing time of 42 days applied to disability pensions. Keva's processing times in respect of all types of pension were shorter by 8–24 days than private pension providers on average.

The number of decisions declined by 0.7% from 2015 (497 decisions). Despite the total number of decisions remaining virtually the same, there were changes within the various benefits.

The greatest increase in relative terms was seen in part-time pension decisions (37.6%). This is explained by part-time pension being discontinued at the start of 2017 as part of the pension reform. A particularly high number of part-time pension decisions was indeed issued in December.

A clear bump (10.1%) was also seen in the number of partial disability

Decisions issued by Keva broken down by pension Act



Total processing time for pension applications, days

Pension benefit	2016	2015	Change, days	Private providers 2016
Old-age pension	20	22	-2	43
Part-time pension	27	19	8	51
Disability pension	42	39	3	66
Survivors' pension	18	10	8	26
Rehabilitation	12	13	-1	29

Source: Finnish Centre for Pensions

Number of all decisions by pension benefit 2016 and 2015

Benefit	2016	2015	Change, %
Old-age pensions	24,983	25,987	-3.9
Full disability pensions	16,090	16,338	-1.5
of which new decisions	5,636	5,844	-3.6
Partial disability pensions	10,003	9,082	10.1
of which new/preliminary decisions	4,076	3,675	10.9
Survivors' pensions	5,896	5,611	5.1
Part-time pensions	3,084	2,241	37.6
Other pension matters	361	426	-15.3
Rehabilition decisions	6,787	8,016	-15.3
Total	**67,204**	**67,701**	**-0.7**

pension decisions, which in recent years have come to account for an increasing proportion of disability pensions. In 2016, 38.3% of all disability pension decisions issued concerned partial disability pension.

The number of survivors' pension decisions increased by 5.1%.

The greatest decrease in the year was seen in the number of rehabilitation decisions (-15.3%). Legislation entering into force at the start of 2015 required pension providers to provide disability pension applicants with a preliminary decision on the right to vocational rehabilitation when the requirements for it were satisfied. This contributed to the higher number of rehabilitation decisions in 2015 and the subsequent levelling off in 2016.

The numbers of decisions on old-age pensions (-3.9%), full disability pensions (-1.5%) and other pension matters (-15.3%) also decreased.

A total of 40,460 decisions were issued on new pension applications and 37,304 of these decisions were favourable. The rejection rate for new disability pension applications was 22.9% (21.4% in 2015). Among private pension providers, the average rejection rate for new disability pension applications was 31.0%. In rehabilitation decisions, 15.3% of those issued by Keva were rejections while the equivalent figure among private pension providers was 19.2%.

The number of applications increased by 4.1% on the year. The highest proportionate increase was seen in applications for part-time pension (59.0%). A higher number of applications than in 2015 were also received for partial disability pension (8.2%), survivors' pension (5.3%) and old-age pension (3.9%).

Online applications accounted for 26% of the total volume (22% in 2015) while 16% (15% in 2015) were forwarded to Keva by local government pension ombudsmen. The My Pension service was used to file 9% of all applications (3% in 2015). Online applications accounted for 58% of all old-age pension applications (50% in 2015).

The number of pension applications has been estimated to remain high in the near future if the number of persons insured for earnings-related pension in the public sector and the structure of this group remains unchanged. No surprises in the volume of pension applications are anticipated on the basis of the age and occupation breakdown of those currently insured. Changes in the operating environment, in particular the health, social services and regional government reform, may have considerable impacts on the number and structure of the insured and thus also on application volumes.

Pension decision rectification procedure

In 2016, Keva processed a total of 1,450 appeals filed with the Pension Appeal Board against its decisions in 'self-rectification procedure'. Of these, 996 had to do with assessment of work capacity. The rectification rate was 13.4% for all appeals and 11.1% for work capacity assessment appeals. The remaining appeals were submitted to the Board for consideration.

In 2016, Keva also processed a total of 204 appeals filed with the Insurance Court against decisions issued by the Pension Appeal Board. Of these, 175 concerned work capacity assessment and the rectification rate among these was 1.1%.

The Pension Appeal Board revised 10% of the rejection decisions issued by Keva subject to appeal. The Insurance Court revised 9.7% of Keva's decisions subject to appeal.

Persons retiring

As expected, the number of persons retiring from the service of local government, the State, the Church and Kela rose only slightly (3.1%) and totalled 21,242.

The average age of the persons retiring was 61.2 (0.2 years higher than in 2015). In 2016, the average age of retiring on old-age pension was 63.7 and old-age retirement accounted for 73.4% of all persons retiring. Persons starting to receive a new partial disability pension are also counted as persons retiring even if they continue working alongside drawing a pension.

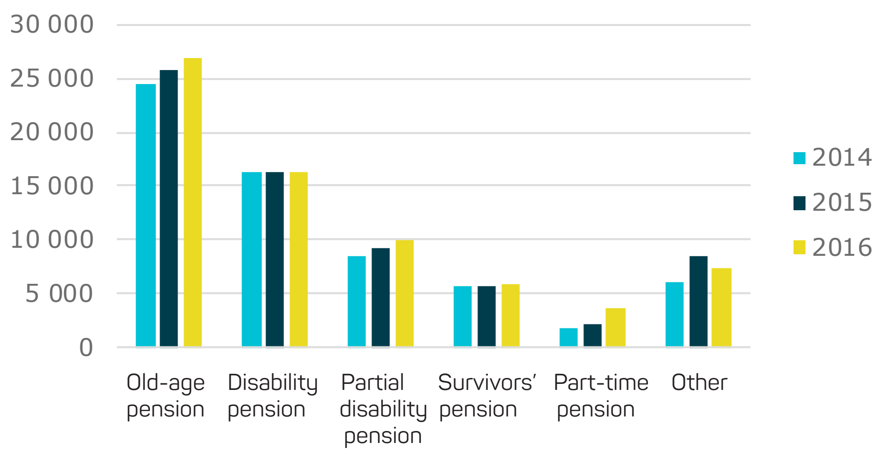
The major reasons for disability were musculoskeletal disorders and mental health problems, which together accounted for 65% of all disability pensions.

The expected effective retirement age for a 25-year-old employee was 61.2 in local government service (61.4 in 2015) and 61.9 in State service (military personnel excluded) (62.3 in 2015). Expected effective retirement age is the age at which employees currently aged 25 would on average retire if future retirement patterns remained exactly the same as in the year under review. The expected effective retirement age for a 25-year-old in the entire earnings-related pension sector was 61.1 in 2016.

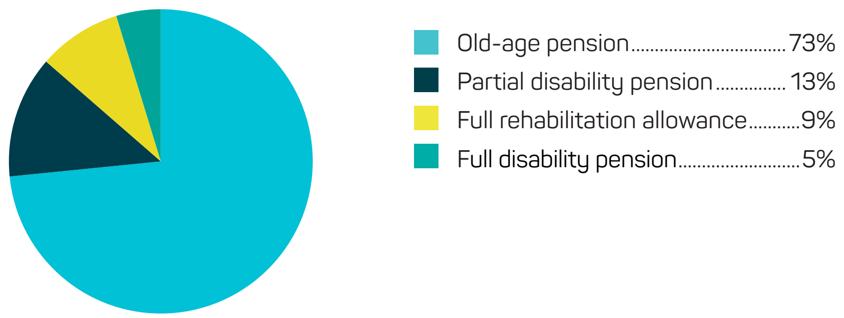
Pensions paid

Pension expenditure under the Local Government Pensions Act was EUR 4,738 million, an increase of EUR 193 million

Number of applications received by Keva by pension benefit



Percentage of persons retiring by pension benefit in 2016



or 4.2% from 2015. At year-end, the number of pension recipients totalled roughly 387,000 or 2% more than in 2015.

In 2016, Keva paid out EUR 4,502 million in State pensions, an increase of roughly EUR 62 million or just over 1% from 2015. At year-end, State pension recipients numbered approximately 259,000, a decrease of just under 2% from 2015. Evangelical-Lutheran Church pensions paid out by Keva amounted to roughly EUR 188 million, an increase of 4% from 2015. The equivalent expenditure on the pensions of Kela's salaried employees came to roughly EUR 96 million, an increase of some 3% from 2015.

The State, the Evangelical Lutheran Church and Kela funded their own pensions by paying to Keva a monthly advance determined by the Ministry of Finance. At the end of the year, this advance was then adjusted against actual pension expenditure. For 2016, Keva will charge an additional EUR 7.3 million to the State and EUR 1 million to the Church. Kela will be refunded roughly EUR 0.06 million. These items were recognised in the financial statements as adjustments to advance payments.

WORKING LIFE SERVICES AND SUPPORT FOR CONTINUING AT WORK

Keva achieved its targets set for the local government and State sectors in respect of support for continuing at work. The percentage of persons retiring at the earliest age of 63 accounted for 62% of all persons retiring in the local government sector and 65% in the State sector. This was 7 and 6 percentage units above target, respectively. The percentage of persons retiring on partial disability pension accounted for 50% of all persons retiring on disability pension in both the local government and the State sector, which was 9 and 12 percentage units above target, respectively.

Keva provided its employer customers working life services comprising consultation on workplace wellbeing and work capacity management, active support, change support, managing disability costs, efficient utilisation of workplace wellbeing surveys, and improving cooperation in occupational health care. Keva also organised training, coaching, seminars and workshops to support workplace wellbeing and work capacity management.

The annual Keva Day was held with a new concept that integrated Keva's earlier approaches to stakeholder events. Focusing on the theme of changes in the operating environment, Keva Day was attended by 550 customers.

Workplace wellbeing promotion grants are a pilot project introduced in the year under review. Designed to support customer projects in this field, the grants focused on the theme of workplace wellbeing and work capacity management. Fifteen of the 47 grant applications were funded. A total of EUR 300,000 has been set aside for the grants in 2016 and each project was allocated the sum of EUR 10,000–15,000. The projects will be monitored and support provided for their mutual networking.

A survey of workplace wellbeing in the public sector, focusing on local government and Evangelical Lutheran Church employees, was conducted in the year under review by Keva together with the Municipal Group of the Centre for Occupational Safety.

The workplace wellbeing survey service provided support for workplace wellbeing management in six local government organisations, where shop stewards were integrated more closely into workplace wellbeing management. An approach in which consultation was built around an workplace wellbeing survey conducted in-house was additionally piloted in one organisation.

The Kaari calculator service estimated the disability costs incurred by local government employers for 35 employer customers. Examined proportionate to the number of persons insured, the service had a coverage of 290,000 persons insured. An analysis of their workplace wellbeing management was furthermore provided to 17 employers.

The work capacity management analysis service piloted an approach in which customers were involved more closely in the performance of the analysis. The generation of calculation analyses and reports by means of in-house, inclusive workshops was piloted with large organisations. The service will be upgraded during 2017 on the basis of these experiences.

The 'Workplace Wellbeing Strategically' coaching develops strategic human resource and workplace wellbeing management. The two coaching courses held in 2016 were attended by 63 persons from 20 organisations.

Going ahead, customer service will to an increasing degree be provided online also when it comes to workplace issues. More calculations of the costs of disability can be provided in the future by means of the new online service. The online workplace wellbeing survey was improved and will in future allow the survey to be provided to an increasing number of customer organisations. A tool developed and piloted evaluating the management of workplace wellbeing and work capacity will be introduced in early 2017 as a support measure in consultation.

A key stakeholder undertaking was the management development project for supervisors and middle management (EKJ) implemented in cooperation with the Association of Finnish Local and Regional Authorities, Local Government Employers KT and FCG. A pilot project aimed at enhancing the workplace wellbeing and work capacity management service provided to major cities was agreed with the City of Helsinki. In addition, a web-based workplace mediation tool was tested in collaboration with the company Sovun Rakentajat Oy. Keva implemented a learning network focusing on the evolving work of supervisors as part of the KunTeko 2020 programme for improving working life in Finnish local government and a learning network related to active support as part of the Evangelical Lutheran Church's equivalent Kirteko programme.

Improvement in the effectiveness of vocational rehabilitation was sought by promoting the start of the rehabilitation process as early as possible. The rehabilitation investigation pilot project launched in 2015 had the aim of identifying persons who would benefit from vocational rehabilitation. The target group in the project were persons whose medical leave had reached 90 days in duration. The project was expanded in autumn 2016 to allow access for all employers. Roughly 50 events on the topic of vocational rehabilitation were arranged for employers and occupational health care providers.

Under a legislative amendment entering into force in 2015, the right of an applicant to vocational rehabilitation as the primary benefit must be ensured in the processing of disability pensions. Keva reformed its internal processes in 2016 such that the person processing a disability pension also issues the decision on the right to vocational rehabilitation when such a decision shall be issued without a separate application, in the context of processing the pension. The reform has improved customer service and the assessment of the customer's overall situation while at the same time allowing the allocation of more resources to ensuring that decisions on the right to vocational rehabilitation also result in the preparation of a plan and thus to the extension of careers.

Over the course of the year, Keva's advisory physicians attended more than 50 consultations, training events and negotiations with occupational health care providers and employers.

Around 200 people took part in the situational reviews provided by Keva for people whose disability pension applications had been rejected.

INVESTMENT OPERATIONS

Very little was expected in the way of investment returns in 2016. The start of the year already saw interest rates at historical lows. The equities market had had a good run of several years since the financial crisis. The capital markets were concerned over global growth and impending political mileposts such as the Brexit referendum, the US presidential election and the Italian constitutional referendum.

All of the above elections turned out the way most feared by the market in advance, yet each succeeding vote brought about lesser and briefer market reactions. At the very end of the year, the capital market appeared to be interpreting the events of the year as 'all good' and investors were rewarded with an unexpectedly positive upswing in returns.

The year 2016 turned out a good one for Keva in terms of investments. Private equity, equity and fixed income investments in particular delivered high returns, while real estate investments and hedge fund investments also performed well. In fact there is cause for happiness with the performance of all asset classes.

At the beginning of 2016, the market value of Keva's investments totalled EUR 40,990 million. At year-end, they had a market value of EUR 44,422 million. The market value of invested capital used to calculate return includes not only the assets mentioned above but also accrued income including accrued interest as well as other items, a total of EUR 4,102 million. Taking these items into account, the market value of invested capital totals EUR 48,524 million. This break-down of imputed returns is used to calculate the break-down for each asset class.

Investments are divided into asset classes, which are fixed-income, equity, real estate, private equity and commodity investments and hedge fund investments. Fixed-income investments consist of loans, bonds and money market investments. The investments are managed in part by Keva and in part by external asset managers. Targeted returns are hedged using derivative instruments, the effects of which on allocation by asset class are taken into consideration in the figures that illustrate the risk-adjusted distribution of investment assets.

Of the different asset classes, the best result was generated by private equity investments (14.5%). Equity investments (listed equities 8.8%) and fixed-income investments (6.5%) delivered excellent performance. Real estate investments (5.0%) and hedge fund investments (3.6%) also performed well.

At year-end 2016, the risk-appropriate market value of Keva's investments broke down as follows: fixed-income investments (including the impact of derivatives) accounted for 45.1%, listed equities for 36.1%, real estate for 6.2%, private equity for 6.4% and hedge funds for 6.2%.

Keva's total investment return at market value after expenses was 7.4% in 2016. The capital-weighted, annual cumulative real return on investments since inception (1988) until the end of 2016 was 4.2%. The non-capital weighted average real return for the same period was 5.4%. The five-year nominal return without capital weighting has been 8.2%, and the real return 7.1%. The ten-year nominal return without capital weighting has been 5.1% and the real return 3.4%.

Fixed income investments

The year in the fixed-income market kicked off with interest rates at exceptionally low levels. The European and US central banks continued to pursue divergent paths in their measures over the course of the year. The European Central Bank had to and will have to continue its accommodative policies while the Fed has already started to tighten its policy. Contrary to expectation the year 2016 turned out to be a very good year in the fixed-income arena.

At year-end 2016, the total market value of Keva's investments in bonds and fixed-income funds stood at EUR 16,621 million. A total of EUR 6,251 million or 37.6% of the bond portfolio was allocated to external asset managers (including funds). The market value return on bonds was 8.8%.

Loans (excluding those granted to Keva companies) totalled EUR 387 million at the end of 2016. This loan portfolio decreased by EUR 70 million during the year. The market value return on these loans was 0.7%.

Other money market investments and deposits totalled EUR 5,058 million at year-end 2016.

A total of EUR 169 million in interest income was recognised for the fixed-income portfolios. The market value return on fixed-income investments was 6.5%.

Investments at fair values 31 Dec 2016

	EUR million	%
Fixed income	22,066	45.5
Equities	17,352	35.8
Real estate	3,002	6.2
Private equity	3,109	6.4
Hedge fonds	2,995	6.2
Total	**48,524**	**100**

Investments by currency at fair values 31 Dec 2016

	EUR million	%
EUR	25,009	51.5
USD	20,088	41.4
JPY	1,850	3.8
GBP	751	1.5
SEK	276	0.6
CHF	235	0.5
Others	315	0.6
Total	**48,524**	**100**

Geographical distribution of investments at fair values 31 Dec 2016

	EUR million	%
Europe (excl. Finland)	15,759	32.5
North America	13,312	27.4
Finland	10,524	21.7
Emerging markets	6,643	13.7
Japan	1,865	3.8
Other	422	0.9
Total	**48,524**	**100**

Equity investments

The market plunges in the early part of 2016 foreboded a year of poor performance, yet spring brought about a bull market that reached its pinnacle at the very end of the year. The market was highly volatile in its responses to elections and referendums but as the year wore on, the market seemed to grow increasingly impermeable to unfortunate turns of events. Ultimately 2016 was a good year in the equities market.

The MSCI index (EUR), which illustrates the average trend of the world's equities, ended up at 11.0% in 2016, compared to 10.5% in 2015. Measured by the Stoxx 600 index, European equities rose by 1.7% (9.6% in 2015). The return on Asian equities (MSCI Asia-Pacific) was 8.3% (9.3%).

At the end of 2016, the total market value of Keva's listed equity investments was EUR 17,352 million. A total of EUR 14,342 million, i.e. 82.7% of the entire equity portfolio, was allocated to external asset managers (including funds).

Dividend income from equity investments totalled EUR 96 million. The market value return on listed equity investments was 8.8%.

Real estate investments

Keva's real estate portfolio consists of direct investments in Finnish and Nordic real estate and real estate shares. The portfolio also includes investments in real estate funds in Finland and abroad, which currently account for roughly one third of all real estate investments.

Keva has sought to reduce the relative share of office buildings in its directly-held portfolio by diversifying into commercial and residential properties. As of 2015, Keva has also been making directly held investments in the other Nordic countries, starting with Sweden.

The market value of real estate and real estate shares was EUR 3,002 million at the end of the year. Real estate funds accounted for EUR 720 million of this sum. A further EUR 200 million was tied up in real estate companies in the form of traditional loans. The amount of investment commitments made in Finnish and foreign real estate funds totalled EUR 1,659 million, with undrawn commitments making up the sum of EUR 480 million.

At year-end 2016, the 127 real estate companies owned by Keva had a total lettable area of approximately 857,000 m^2. There were 4,082 leases in place delivering a net rental income of EUR 100 million. The market-value return on direct real estate investments stood at 4.6% while the return on direct real estate investments calculated on the basis of the Finnish Institute for Real Estate Economics' KTI Index was 4.8%.

The market value return on all real estate investments was 5.0%.

Private equity and hedge fund investments

The private equity investment environment remained favourable in 2016 despite the challenging overall market situation. For hedge funds, the environment was more challenging than before, as was the case in 2015 as well, and returns indeed failed to reach long-term levels.

At the end of the year, Keva's private equity investments totalled EUR 3,109 million (market value) inclusive of investments in unlisted companies. The market value of hedge fund investments totalled EUR 2,995 million at year-end. The amount of investment commitments made to private equity investments totalled EUR 6,843 million, with undrawn commitments making up the sum of EUR 3,361 million.

The market-value return on private equity investments was 14.5%. Hedge fund investments delivered a return of 3.6%.

Investment strategy

Keva's strategy determines the central principles for funding the local government pension system, and the strategic objectives set for the investment operations are derived from these.

The Board of Directors manages Keva's long-term investment activities through the investment strategy. In the shorter term, the Board of Directors manages the investment activities for a given year through an approved investment plan which also includes investment authorisations.

The investment strategy sets out the principles and procedures that will help to achieve the targets set for investment operations in the financial strategy. Most importantly, the investment strategy determines the principles to be followed in the steering of the investment activities.

The Board of Directors of Keva approved the current investment strategy on 8 May 2014. In spring 2016, preparation of a new investment strategy was launched by a new unit established in Keva's investment function.

Responsible investing

The returns to cover pension liability are driven by economic growth and arise in the long term. Sustainable economic development is integral to the pursuit of long-term gains.

Keva's Board of Directors has decided on the key principles of social responsibility to be complied with in Keva's investment operations. The Board of Directors has also outlined the ways of working and procedures to be used to ensure that social responsibility is integrated into the investment process.

The Board receives regular reports on the realisation of social responsibility in investment operations. Keva also uses data from external social responsibility assessment providers to supplement its own approaches.

The investment strategy unit established in the investment function in 2016 is tasked with developing Keva's responsible investment operations as part of the investment strategy process.

SUBSIDIARIES AND ASSOCIATED COMPANIES

At year-end 2016, Keva owned in whole or in part a total of 126 Finnish real estate companies, the same number as a year earlier. Keva owned 105 real estate companies in full and had a majority holding in 10 others. There were five associated companies (holding of 20-50%), and six real estate companies where Keva's holding was less than this. In addition, Keva held 98% of a company set up in Sweden to manage real estate investments in that country.

In addition to real estate companies, Keva held the entire capital stock of Kuntasijoitus Oy KE, a 30.66% stake in Municipal Finance Plc and a 25.5% stake in Exilion Capital Oy, which is the general partner in the Exilion Real Estate I Ky fund.

PENSION LIABILITY FUND

The difference between Keva's annual income and expenditure is added to or deducted from the pension liability fund. At year-end 2016, the fund stood at EUR 48,635 million, which was EUR 3,686 million (8.2%) higher than a year earlier.

PRESENT VALUE OF ACCRUED BENEFITS IN KEVA MEMBER ORGANISATIONS' PENSION SYSTEM

Based on the provisions of pension legislation, the value of the benefits that have accrued in the pension system of Keva's member organisations but which have not yet been paid out clearly exceeds the value of the pension liability fund. The present value of the accrued benefits was estimated to have been EUR 111 billion at year-end 2015. This estimate is approximately EUR 6 billion higher than the earlier estimate owing to factors which include taking account of the mortality rate in Statistics Finland's new population forecast and the introduction of new register materials. During 2016, the value increased by EUR 2 billion to EUR 113 billion.

Since the value of the pension liability fund in 2016 grew by more than the present value of benefits, the present value of unfunded benefits decreased by EUR 2 billion during the year.

The present value of accrued benefits is estimated based on the best available information on mortality rate and other trends. However, this is just an indicative estimate of the current situation of the pension system and changes in the assumptions used in calculation may alter it significantly.

OPERATING COSTS, DEPRECIATION AND STATUTORY PAYMENTS

Operating costs and depreciation before payments received (gross operating costs) in 2016 totalled EUR 79.6 million, which is EUR 8.1 million or 9.2% less than in 2015.

The largest individual cost item was personnel costs, which were EUR 39.9 million, EUR 0.7 million or 1.7% less than in 2015. Other operating costs decreased by EUR 7 million or 17.2% compared to the previous year. The most significant contributing factor was the decrease in IT costs by EUR 4.4 million to EUR 20.5 million. Asset management and custody fees also decreased by roughly EUR 3 million owing to a change in the way of managing investments.

Keva received reimbursements for operating costs and depreciation totalling around EUR 19.2 million (EUR 22.4 million in 2014) for the management of other than local government pensions. Of this sum, the State paid around EUR 16.1 million, the Evangelical-Lutheran Church around EUR 2 million and the Social Insurance Institution of Finland Kela around EUR 0.6 million. Reimbursements were lower than in the previous year due to an overall decrease in Keva's costs and the decline in the share of the State, the Evangelical-Lutheran Church and Kela of all occurrences of retirement managed by Keva.

Keva's net operating costs, including reimbursements received, reflect the costs of implementing local government pensions. Net operating costs were EUR 60.4 million, which is EUR 4.9 million or 7.5% less than in the previous year.

When examined by function, the gross costs of pension operations were EUR 46.9 million, roughly 9% less than in the previous year. Taking into account reimbursements received, the costs of pension operations decreased by approximately 6%. The costs of investment operations were EUR 15.8 million, around 16% less than in 2015. No reimbursements were allocated to investment operations. Gross operating costs for administration were EUR 17 million, around 3% less than in the previous year. Taking into account reimbursements received, the operating costs for administration decreased by just under 1%.

Capital expenditure concerned mainly IT software and hardware and came to EUR 1.8 million, which was EUR 0.5 million less than in the previous year. The most significant IT expenditure involved the development of e-services and the system modifications necessitated by the pension reform of 2017.

Planned depreciation in 2016 came to EUR 5.9 million, EUR 0.4 million less than in 2015.

Statutory payments refer to Keva's share of the costs of the Finnish Centre for Pensions, the Pension Appeal Board and the Financial Supervisory Authority. These costs totalled EUR 8.2 million, EUR 0.5 million less than in 2015. Around EUR 2.3 million of these costs were paid by the State, Evangelical Lutheran Church and Kela.

All told, Keva received EUR 21 million in reimbursements from the State, Evangelical Lutheran Church and Kela, which was EUR 3.4 million less than in 2015.

ADMINISTRATION

Keva's highest decision-making authority is the Council, the members of which are appointed by the Ministry of Finance for the municipal electoral period. The Council consists of 30 members, 26 of whom are appointed according to a proposal by the Association of Finnish Local and Regional Authorities, which is based on the results of the municipal elections. Four members are appointed based on a proposal by the main municipal negotiating organisations. The term of the current Council started in 2013 and under the provision on the entry into force of the Keva Act, it will extend until the end of August 2017.

The Council was chaired by Mr Harri Jokiranta of Seinäjoki and the Deputy Chair was Ms Maarit Ojavuo of Kajaani.

The Council convened for four meetings during the year under review. The attendance rate of the Council's regular members was 88%. When the attendance of deputy members is included, the attendance rate was 95%. The Council members are paid an attendance fee of EUR 400 per meeting, in addition to which the chair and deputy chair are paid an annual fee of EUR 9,000 and EUR 8,000, respectively. Attendance fees to Council members totalled EUR 70,575.

Keva's administration is the responsibility of the Board of Directors, which the Council elects for a two-year term of office. The Board elected for the 2015–2016 term of office was chaired by Ms Anna-Kaisa Ikonen, mayor of Tampere. Mr Kari Nenonen, Mayor of Vantaa served as deputy chair. Other Board members were Ms Heini Jalkanen, Business Director; Ms Sallamaari Muhonen, communications consultant; Mr Harri Virta, managing director; Mr Raimo Vistbacka LLM; Mr Markus Lohi, Member of the Finnish Parliament; Mr Risto Kangas, Director at the Negotiation Organisation for Public Sector Professionals (JUKO); and Ms Päivi Niemi-Laine, Chief Executive Officer at the Union of Local Government Employees. Under the new Keva Act, the term of office of the current Board of Directors expires at the end of August 2017.

The Board of Directors convened 13 times during the year under review. The attendance rate of the Board's ordinary members was 90%. When the attendance of deputy members is included, the attendance rate was 97%. The Council's chair and deputy chair also have the right to attend and speak at Board meetings. Board members receive an attendance fee of EUR 400 for meetings, in addition to which the chair receives an annual fee of EUR 18,000, the deputy chair EUR 10,000 and members EUR 8,000. Board members were paid total attendance fees of EUR 64,800.

In addition to the Board of Directors and Council, Keva's statutory bodies include the Investment Advisory Committee, the members of which are appointed by the Board for its term of office. The Investment Advisory Committee includes representatives of municipal negotiating organisations, the Ministry of Finance and the Ministry of Employment and the Economy. Mr Seppo Juntti, Financial Director, City of Salo, served as chair of the Investment Advisory Committee and Ms Terttu Savolainen, Director of the Regional Administrative Agency of Northern Finland, served as deputy chair. The Investment Advisory Committee did not convene during the year under review. The term of the current Committee is the same as that of the Board and it expires at the end of August 2017.

The Working Life Development Working Group is a body defined in the Standing Orders that is tasked with developing measures to maintain the health and work capacity of municipal employees. Of the 12 working group members, six are chosen on the basis of proposals by the main municipal negotiating organisations. The Working Life Development Working Group was chaired by Mr Aki Lindén, Chief Executive Officer of the HUS Joint Authority. The Group convened for three meetings during the report year. The term of the current Group is the same as that of the Board and it expires at the end of August 2017.

Mr Tapani Hellstén served as acting CEO in the early part of the year under review. At its meeting of 16 February 2016 the Council appointed Mr Timo Kietäväinen MScSocSc as Keva's new CEO and he assumed the post on 1 May 2016.

Mr Tapani Hellstén and Mr Kimmo Mikander served as deputy CEOs. Mr Hellstén's primary area of responsibility is pension and working life services while Mr Mikander is responsible for customer relations.

The CEO is provided support in managing Keva by the management group which convenes on a regular schedule. The management group prepares matters for submission to the Board and considers also other issues central to the management and planning of operations. The management group convened for 40 meetings in the year under review. In 2016, the management group was chaired by CEO Timo Kietäväinen (until 30 April 2016 acting CEO Tapani Hellstén) and its members comprised deputy CEOs Tapani Hellstén and Kimmo Mikander, CIO Ari Huotari, CFO Tom Kåla, Paula Sivunen, acting head of the shared services function, and staff representative, shop steward Pasi Lehto. Compliance officer Markus Mankin serves the group's secretary.

PERSONNEL

At year-end 2016, Keva employed 540 people (546 at year-end 2015), of whom 20 (16 in 2015) were fixed-term employees. Women accounted for roughly 70% of Keva's personnel and the average age of employees was 49.2.

One of the focal areas in the Keva 2019 projects was building on Keva's corporate culture. This undertaking entails reforms in areas including management, personnel policies, premises and e-approaches. The project also makes use of internal agents of change.

The statutory employer/employee negotiations on the reform of Keva's management system and organisation took place in autumn 2016. The aim of the reorganisation was to respond to the challenges presented to Keva by the change in the operating environment. The reorganisation resulted in customer relationships and shared services being integrated into a matrix function for customer relationships and services. The HR unit, communications unit and stakeholder cooperation, and risk management and internal audit started to report directly to the CEO. A new post of communications director was established in the communications unit. The changes entailed no job losses.

In 2016, personnel were provided with a diverse range of training and coaching. The pension reform was a particular focus in the enhancement of expertise. Training was also provided in support of teamwork, digital skills and customer orientation, and knowledge of administrative legislation. Communications training centred on social media skills. Training in the Office 2016 software and the cloud office system was also provided.

Supervisory work was supported by means of supervisor training and other events, where the themes included the Keva 2019 projects, lean thinking, and employment and occupational health and safety matters.

The Sympa HR system was introduced in May. As in 2015, the goal in performance appraisals was to establish four personal objectives and also to review the accomplishment of the previous year's objectives.

No distinct job satisfaction survey was conducted in 2016. A workplace environment survey, reputation survey and workplace survey were conducted in the autumn as well as a health survey among a portion of the personnel. The development measures arising from the personnel survey conducted in 2015 were continued.

On 1 May 2016, Terveystalo replaced long-term partner Mehiläinen as Keva's occupational health care services provider.

As in earlier years, workplace wellbeing was supported through a wide range of personnel clubs. Keva also offers its employees exercise and culture vouchers as well as employer-subsidised commuter tickets. An active support model is in place for the purpose of maintaining work capacity.

IT MANAGEMENT

The focus in pension system development in 2016 was on implementing the statutory modifications to the information systems necessitated by the pension reform of 2017. Most of the information system modifications relating to the pension reform took place in the information systems maintained by Arek Oy. The project was successful and the required modifications were made operational to schedule.

The development of digital services was a focus area for Keva. Our customers have found the new online pension application service introduced in autumn 2016 to be clear and easy to use. The new contribution system for calculating and invoicing employer contributions inclusive of its online services as well as the new online services for small employers to report employment details were made operational in January. The Keva website and the online services for employers were built on a new platform.

Preparations for putting the pension payments system up to tender as required under the Public Procurements Act were initiated. The current system is approaching the end of its lifecycle and will be replaced with a state-of-the-art system that includes features to permit e.g. increasingly automated processing.

The Office 365 suite was introduced in the year under review. The cloud-based suite will enhance the effective utilisation of various terminal devices and enable more efficient remote work.

INTERNAL CONTROL

Internal control means all the procedures, systems and methods through which Keva's management aims to ensure efficient, economical and reliable operations. Besides daily supervisory control, risk management and compliance as well as internal auditing are also key fundamentals of internal control.

Risk management

General development of risk management

The focus in the general development of risk management in 2016 was on strengthening the integration of the risk management process with the processes for the planning, steering and management of operations and on continuing the rollout of the risk management process at various levels of the organisation. Risk surveys were reported to the CEO and the management group at six-month intervals. Monitoring and reporting procedures in the risk management process as well as the related technical support were further improved and documentation was supplemented.

In order to further improve data security and data protection, Keva continued to develop the principles, approaches and processes as well as risk analyses relating to operations. The data security level of IT systems was tested regularly through data security audits. Another focus area was preparing for the entry into force of the new EU Data Protection Regulation.

Aspects improved in Investment Operations' risk management included risk reporting, authority and limit monitoring, investment processes and the associated documentation.

Contingency plans

In order to ensure uninterrupted operations Keva has in place a facility-level contingency plan approved by the Board of Directors as well as complementary contingency plans for each function approved by the management group.

Most significant risks

The ultimate impacts of the decisions made in the restructuring underway in the public sector and the health, social services and regional government reform remain to be determined as yet but even now the reforms may already be judged to be potentially significant to Keva's operations and to Keva's legal standing and role as a public sector pension provider. These considerations are also reflected in the strategic risks to which Keva is exposed.

Keva estimates the biggest long-term strategy risk to be a decrease in the number of employees covered by the Local Government Pensions Act and the ensuing significant deterioration in the funding base in the long term. The funding base may be eroded if the number of people insured under the Local Government Pensions Act declines as a result of the incorporation or outsourcing of municipal services. This in turn may give rise to pressure to raise the pension contribution. The uncertainty factors relating to the health, social services and regional government reform as well as any eventual changes in the manner in which municipal services are provided serve to further highlight the significance of the risk in the long term.

Keva also considers that long-term returns on investments failing to achieve the target level specified in the investment strategy could constitute a major strategic risk. The target level is defined based on the funding situation in the earnings-related pension system at any given time. From the investment perspective, the market environment remained challenging. The capital-weighted, long-term real return on investments between 1988 and 2016 was 4.2%.

Keva assesses its medium-sized strategic risks to be associated with the management and administration of Keva and with customer satisfaction. Major projects aimed at reforming the management system and management culture as well the organisation in response to the challenges arising from changes in the operating environment, the foremost among these being the health, social services and regional government reform, were initiated in 2016.

The most significant operative risks had to do with personnel, operating processes, information systems and information security, and the management of projects and undertakings.

Market risk and liquidity risk

The fluctuation of market values is a short-term investment risk. This risk can be illustrated with the Value at Risk figure (VaR). The VaR figure for Keva's investments calculated on the basis of monthly returns during a two-year period was EUR 1,495 million at the end of 2016, which means that with a 97.5% probability, this is the biggest possible loss on the entire investment portfolio within the time span of one month. The VaR figure at the end of the previous year was EUR 1,223 million. The VaR figure has risen slightly because annual volatility has increased (6.4%) when compared to the previous year (6.0%).

Since Keva's contribution income exceeded pension expenditure, liquidity risk was of little significance.

Compliance

Keva has in place an independent Compliance function tasked with providing support to management and the entire organisation in ensuring compliance with good governance and the external and internal rules relating to operations. In accordance with an action plan approved by the Board of Directors, Compliance monitors Keva's operations for compliance with legislation, statutory regulations and internal guidelines. The function also provides advise and guidelines in the interests of strengthening trust in Keva's operations and reinforcing a responsible corporate culture. Compliance additionally monitors legislative changes relating to operations and the operating environment and provides management with support in making preparations for these. The Compliance function operates under a charter adopted by the Board of Directors.

Insider guidelines

Keva has in place insider guidelines adopted by the Board of Directors.

Internal audit

The internal audit is a component in Keva's system of control and supervision that serves as an aide to the CEO and provides support to the Board of Directors in their supervision duties. Internal audit is tasked with providing an independent and objective assessment of Keva's operations and processes in terms of the effectiveness, efficiency and adequacy of risk management, internal control and management and administrative procedures, and issuing recommendations for improvement. The internal audit function's activities are based on the operating plan for internal auditing adopted each year by the Board of Directors. In accordance with the internal audit charter, the function reports to the CEO and the Board of Directors on the audits carried out and the conclusions made.

OUTLOOK

The pension reform will have the effect of retarding the rise in pension expenditure in public sector pension systems.

The more specific provisions to govern the freedom of choice of customers integrated into the health, social services and regional government reform are yet to be drafted and the impacts of freedom of choice on payrolls in service provision and thus also the pension system of Keva's member organisations is difficult to estimate as yet. The transitional pension system arrangements being prepared as part of the reform will help control the effects of the reform on pension funding but it is too early to estimate the level of contributions required in the near future in the pension system of Keva's member organisations.

The health and social services reform will have a profound impact on municipalities. At the start of 2019, employees of municipalities, joint municipal authorities and regional state government will transfer into the employ of the counties that will be established at that time. It has been estimated that the counties would assume roughly 6,000 regional state government employees and approximately half of the 520,000 persons insured under the pension system of Keva's member organisations.

The reform is likely to result in a review as to the future viability of separate pension systems for Keva's member organisations and the private sector. The working group on this topic will start its work in spring 2017 and it is expected to submit its report in summer 2018.

Many new solutions are likely to be introduced in the provision of services beyond social and healthcare services, and the powerful interest of the private sector to enter the wide local government services market is likely only to intensify. Pressures towards adjustment of local government finances remain in play and the annual attrition of 16,000 insured persons taking retirement will provide opportunities not only for adjustment but also for private sector services.

The earnings-related pension system is involved in the income register project underway under the leadership of the tax authorities. The primary point of departure for the project is to facilitate filing processes for employers. The project includes numerous challenges and compromises from the earnings-related pensions perspective but when implemented, it will fundamentally shape the operations of earnings-related pension providers and also enable the innovation of entirely new services.

As things stand now, the pension system of Keva's member organisations will switch over in the current year to using the returns on funds to pay for pensions. This will usher in a new era for investment operations with the enhanced focus on the liquidity of investments.

From the pension investor's perspective the near future seems all the more of a challenge. While growth appears to have picked up in the global economy, problems may yet arise from the policies of the new administration in the US, for example. Rising interest rates make fixed-income investments less attractive but the timing of the upswing in the various markets is hard to gauge. The prospect of protectionism is casting a shadow over the development of the world economy and has served only to increase the uncertainties relating to equities. Going ahead, it is very likely that investing operations will be faced with greater uncertainty and lower returns.

APPENDIX: PENSION ACT-SPECIFIC CHARTS

Total pension application processing time (days) and service level 2016

Pension benefit	KuEL	VaEL	KiEL	KelaL	Private providers
Disability pensions	41	41	59	40	66
Old-age pensions	20	17	22	16	43
Part-time pensions	27	30	26	38	51
Survivors' pensions	19	16	24	54	26
Rehabilitation promises	13	13	11	9	29
Service level	92.7	94.8	93	93.2	..

Source for processing times: Finnish Centre for Pensions

Application rejection rates 2016

Application	KuEL	VaEL	KiEL	KelaL	Private providers
New disability pension	23.4	18.9	26.2	18.2	31.0
Rehabilitation	14.7	20.5	18.2	21.4	19.2

Source: Finnish Centre for Pensions

Pension decision rectification procedure 2016

	KuEL	VaEL	KiEL	KelaL
Self-rectified by Keva				
No. of appeals against Keva's decisions	1,100	301	38	11
Rectification rate (%) of all appeals	14.1	11.0	13.2	9.1
No. of appeals concerning work capacity assessment	818	139	30	9
Rectification rate (%) of appeals concerning work capacity assessment	12.2	6.5	3.3	11.1
No. of appeals against decisions of the Pension Appeal Board	159	39	6	0
Rectification rate (%) of all appeals	2.5	0	0	0
No. of appeals concerning work capacity assessment	140	29	6	0
Rectification rate (%) of appeals concerning work capacity assessment	1.4	0	0	0
Decisions by appeal bodies				
No. of appeals resolved by the Pension Appeal Board	760	179	11	-
Decisions revised, %	9.5	10.1	9.1	-
No. of appeals resolved by the Insurance Court	179	52	7	-
Decisions revised, %	8.9	9.6	28.6	-

Number of pension applications under KuEL by pension benefit 2016 and 2015

Pension benefit	2016	2015	Change, %
Åld-age pensions	19,126	18,038	6.0
Full disability pensions	13,956	13,795	1.2
Partial disability pensions	8,507	7,751	9.8
Survivors' pension	2,887	2,711	6.5
Part-time pensions	2,641	1,674	57.8
Partial early old-age pensions	116	0	..
Total	47,233	43,969	7.4

Number of pension applications under VaEL by pension benefit 2016 and 2015

Pension benefit	2016	2015	Change, %
Old-age pensions	6,653	6,753	-1.5
Full disability pensions	1,788	1,952	-8.4
Partial disability pensions	1,102	1,104	-0.2
Survivors' pensions	2,785	2,687	3.6
Part-time pensions	812	508	59.8
Partial early old-age pensions	32	0	..
Total	13,172	13,004	1.3

Number of pension applications under KiEL by pension benefit 2016 and 2015

Pension benefit	2016	2015	Change, %
Old-age pensions	885	837	5.7
Full disability pensions	473	519	-8.9
Partial disability pensions	164	155	5.8
Survivors' pensions	186	169	10.1
Part-time pensions	74	44	68.2
Partial early old-age pensions	3	0	..
Total	1,785	1,724	3.5

Number of pension applications under KelaL by pension benefit 2016 and 2015

Pension benefit	2016	2015	Change, %
Old-age pensions	187	205	-8.8
Full disability pensions	93	82	13.4
Partial disability pensions	141	143	-1.4
Survivors' pensions	47	43	9.3
Part-time pensions	48	23	108.7
Partial early old-age pensions	3	0	..
Total	519	496	4.6

Number of all decisions by pension benefit 2016 and 2015, KuEL

Pension benefit	2016	2015	Change, %
Old-age pensions	17,737	18,117	-2.1
Full disability pensions	13,779	13,729	0.4
of which new decisions	4,825	4,908	-1.7
Partial disability pensions	8,564	7,686	11.4
of which new or preliminary decisions	3,491	3,120	11.9
Survivors' pensions	2,887	2,706	6.7
Part-time pensions	2,303	1,663	38.5
Other pension matters	335	363	-7.7
Rehabilitation decisions	6,047	7,066	-14.4
Total	**51,652**	**51,330**	**0.6**

Number of all decisions by pension benefit 2016 and 2015, VaEL

Pension benefit	2016	2015	Change, %
Old-age pensions	6,267	6,818	-8.1
Full disability pensions	1,760	2,004	-12.2
of which new decisions	608	689	-11.8
Partial disability pensions	1,132	1,100	2.9
of which new or preliminary decisions	458	431	6.3
Survivors' pensions	2,782	2,692	3.3
Part-time pensions	672	515	30.5
Other pension matters	26	63	-58.7
Rehabilitation decisions	538	738	-27.1
Total	**13,177**	**13,930**	**-5.4**

Number of all decisions by pension benefit 2016 and 2015, KiEL

Pension benefit	2016	2015	Change, %
Old-age pensions	816	840	-2.9
Full disability pensions	460	525	-12.4
of which new decisions	176	220	-20.0
Partial disability pensions	167	154	8.4
of which new or preliminary decisions	72	60	20.0
Survivors' pensions	180	171	5.3
Part-time pensions	63	42	50.0
Other pension matters	0	0	
Rehabilitation decisions	143	176	-18.8
Total	**1,829**	**1,908**	**-4.1**

Number of all decisions by pension benefit 2016 and 2015, KelaL

Pension benefit	2016	2015	Change, %
Old-age pensions	163	212	-23.1
Full disability pensions	91	80	13.8
of which new decisions	27	27	0.0
Partial disability pensions	140	142	-1.4
of which new or preliminary decisions	55	64	-14.1
Survivors' pensions	47	42	11.9
Part-time pensions	46	21	119.0
Other pension matters	0	0	..
Rehabilitation decisions	59	36	63.9
Total	**546**	**533**	**2.4**

Number of persons taking retirement by pension benefit 2016

Pension benefit	KuEL	VaEL	KiEL	KelaL
Old-age pension	10,547	4,442	493	113
Full disability pension	840	128	32	6
Full cash rehabilitation benefit	1,619	201	55	11
Partial disability pension	2,354	316	42	43
Total	**15,360**	**5,087**	**622**	**173**

Average age of persons taking retirement by pension benefit 2016

Pension benefit	KuEL	VaEL	KiEL	KelaL
Old-age pension	64.1	62.8	64.4	64.7
Full disability pension	58.0	57.5	59.2	59.9
Full cash rehabilitation benefit	49.1	49.9	47.9	45.8
Partial disability pension	56.2	56.2	56.1	54.0
Total	**60.9**	**61.8**	**62.1**	**60.7**

Governing bodies 2016

COUNCIL IN THE TERM OF 1 JAN 2013–31 AUG 2017

Members	Personal deputies	Members	Personal deputies
Chair, Mr Harri Jokiranta Seinäjoki	Ms Pilvi Torsti Helsinki	Mr Markku Koski Sievi	Ms Kirsi Torikka Savonlinna
Deputy Chair Ms Maarit Ojavuo Kajaani	Mr Risto Ervelä Sauvo	Ms Outi Kuismin Oulu	Ms Marja Lähde Oulu
Ms Miia Antin Hattula	Ms Jonna Heikkilä Nakkila	Mr Petri Lindroos JUKO ry	Mr Jarmo Niskanen JUKO ry
Ms Diana Bergroth-Lampinen Pori	Mr Jukka Nyberg Kouvola	Mr Saku Linnamurto Savonlinna	Mr Pekka Leskinen Leppävirta
Ms Christina Båssar Korsnäs	Mr Christian Sjöstrand Helsinki	Ms Marja Lounasmaa Kunta-alan unioni ry	Ms Päivi Ahonen Kunta-alan unioni ry
Ms Piia Flink-Liimatainen Äänekoski	Mr Tommy Björkskog Naantali	Mr Leo Lähde Nokia	Mr Hannu Kokko Vantaa (until 16 Feb 2016) Mr Teemu Meronen Helsinki (from 1 Mar 2016)
Mr Keijo Houhala KTN ry	Ms Leila Lehtomäki KTN ry		
Ms Riitta Jakara Orivesi	Mr Toni Eklund Turku	Mr Juhani Nummentalo Salo	Mr Ismo Pöllänen Imatra
Ms Paula Juka Muhos	Mr Jaakko Uuksulainen Kitee	Mr Lauri Nykänen Tornio	Ms Virpi Takalo-Eskola Oulainen
Mr Harri Kerijoki Heinola	Ms Maarit Markkula Köyliö	Ms Helena Ojennus Parkano	Mr Simo Riuttamäki Huittinen
Mr Niko-Tapani Korte Kuopio	Ms Sinikka Hälli Joensuu	Ms Silja Paavola KoHo ry	Mr Jukka Maarianvaara KoHo ry

Members	Personal deputies
Mr Markku Pakkanen Kouvola	Ms Pauliina Takala Muurame
Ms Terhi Peltokorpi Helsinki	Mr Topi Heinänen Ruokolahti
Ms Ulla Perämäki Muurame	Mr Markku Turkia Mikkeli
Mr Antti Rantalainen Hyvinkää	Mr Arto Ojala Kemijärvi
Mr Aki Räisänen Kajaani	Ms Maija Jakka Vihti
Mr Jorma Räsänen Kaavi	Ms Minna Sarvijärvi Ylöjärvi
Ms Tiina Sarparanta Kajaani	Ms Salla Rundgren Vaasa
Ms Pia Sääski Askola	Mr Jorma Liukkonen Kouvola
Ms Elise Tarvainen Saarijärvi	Ms Aulikki Sihvonen Kontiolahti

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Deputy Chair Mr Kari Nenonen Vantaa	Ms Tarja Filatov Hämeenlinna
Ms Heini Jalkanen Naantali	Mr Juha Kuisma Lempäälä
Mr Risto Kangas JUKO ry	Ms Anne Sainila-Vaarno KoHo ry
Ms Sallamaari Muhonen Helsinki	Mr Jani Moliis Helsinki until 12 Jan 2016 Mr Hannu Kokko Vantaa from 16 Feb 2016
Ms Päivi Niemi-Laine Kunta-alan Unioni ry	Mr Rauno Vesivalo KoHo ry
Mr Markus Lohi Rovaniemi	Ms Tuula Partanen Lappeenranta
Mr Harri Virta Tammela	Ms Oili Heino Pori
Mr Raimo Vistbacka Alajärvi	Ms Marke Tuominen Äänekoski

INVESTMENT ADVISORY COMMITTEE IN THE TERM 1 JAN 2015–31 AUG 2017

Members	**Personal deputies**
Chair Mr Seppo Juntti	Ms Jonna Sillman-Sola
Deputy Chair Ms Terttu Savolainen	Ms Sinikka Malin
Ms Ritva Fransman	Mr Tero Ristimäki
Ms Tuulia Hakola-Uusitalo	Mr Tuomo Mäki
Ms Marja Isomäki	Ms Auli Valli-Lintu
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Mr Jouko Narikka	Mr Juha Majanen
Mr Kari Parkkonen	Ms Tiina Ingman
Mr Mika Periaho	Mr Jan Saarinen
Mr Olavi Ruotsalainen	Ms Sisko Seppä

WORKING LIFE DEVELOPMENT WORKING GROUP 1 JAN 2015–31 AUG 2017

Members

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Mr
Aki Lindén

Mr
Kari Hakari

Mr
Tapani Hellstén

Mr
Risto Kangas

Mr
Jukka Kauppala

Ms
Marja Lounasmaa

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Ms
Helena Metsälä

Ms
Anne Mironen

Ms
Merja Paananen

Mr
Tapio Ropponen

Ms
Anne Sainila-Vaarno

Working Group Secretary
Mr
Pauli Forma

ORGANISATION AT 31 DEC 2016

CEO
Mr Timo Kietäväinen

Risk Management and Internal Audit
Head of Internal Audit
Ms Päivi Alanko

Customer Relationship Management

Deputy CEO
Mr Kimmo Mikander

CRM Unit
Customer Relationship Manager
Ms Jaana Kekäläinen

CRM Development Unit
Customer Relationship Development Manager
Mr Tero Manninen

Advisory Services Unit
Customer Services Manager
Ms Taina Uronen

Pension and Working Life Services

Deputy CEO
Mr Tapani Hellstén

Pensions Unit
Pensions Director
Ms Eija Korhonen

Disability Pensions Unit
Pensions Director
Ms Merja Paananen

Insurance Medicine and Rehabilitation Unit
Director of Medical Affairs
Mr Tapio Ropponen

Working Life Services Unit
Working Life Services Director
Mr Pauli Forma

Investments

CIO
Mr Ari Huotari

Internal Equity Unit
CIO, Internal Equity
Mr Fredrik Forssell

External Equity Unit
CIO, External Equity
Ms Maaria Eriksson

Alternative Investments Unit
CIO, Alternative Investments
Mr Markus Pauli

Real Estate Unit
CIO, Real Estate
Mr Petri Suutarinen

Investment Strategy Unit
CIO, Investment Strategy
Mr Jussi Karhunen

Loans and Investment Management Unit
CIO (secondary duty)
Mr Ari Huotari

Financing, Financial and Risk Management

CFO
Mr Tom Kåla

Pension Payments Unit
Pensions Director
Ms Anneli Kajas-Pätäri

Financial Unit
Financial Manager
Mr Olli Pasanen

Securities Administration Unit
Head of Securities Administration
Ms Johanna Haukkovaara

Middle Office Unit
Head of Middle Office
Mr Juha Soininen

Financing Unit
Director of Finance
Mr Allan Paldanius

Shared Services

Acting Head of Shared Services
Information Technology Director
Ms Paula Sivunen

HR Unit
HR Director
Mr Mika Gylén

Communications Unit
Communications Manager
Mr Jouni Kempas

Internal Services Unit
Work Environment Manager
Ms Kristina Vuorela

Legal Affairs Unit
Director of Legal Affairs
Ms Karoliina Kiuru

IT Unit
Information Technology Director
Ms Paula Sivunen

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