

Swedish Code of Corporate Governance

Stockholm 2005

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Printed by Elanders Gotab AB
Stockholm 2005

ISBN 91-38-22308-2
ISSN 0375-250X

Foreword

This document marks the first time that a comprehensive code of corporate governance likely to achieve general acceptance in the business community, has been issued in Sweden. The Code is based on the Swedish Companies Act [aktiebolagslagen(1975:1385)] and the tradition of self-regulation, which from an international perspective, is relatively well-advanced in a number of respects. Nevertheless, it is the opinion of the Code Group that corporate governance in Swedish companies needs to be improved. Like a number of other countries, Sweden has suffered several corporate scandals that have aroused considerable attention and caused legitimate criticism. A large majority of the Swedish people currently own shares, directly or indirectly. How companies listed on the stock exchange are managed affects them materially. Our society is ultimately dependent on a business sector that is dynamic, creates value and enjoys public confidence.

In recent years corporate governance issues have attracted increasing attention both in Sweden and abroad. In various countries important initiatives have been taken by many companies, by governments and at an international level. Many countries, not least in Europe, have established corporate governance codes in the past few years. There are many indications that the field of corporate governance will continue to evolve rapidly. Against this background, the Code Group believes that it is important that Sweden also adopt a corporate governance code. The aim is to improve corporate governance through better selfregulation. In future, members of the business community are to oversee and develop the Code. The Code Group has had ambitious goals. The aim is not only to codify what is currently considered good practice for corporate governance in Swedish companies, but also to advance practice in certain areas.

Work on the Code has taken place in two stages. In the first stage, the work was conducted by a working group composed of nine

members, three of whom were appointed by the Commission on Business Confidence (Förtroendekommissionen) and there maining six by a number of bodies and organisations in the business sector. The work was carried out between October 2003 and April 2004. The proposals put forward by the working group were then widely circulated for comments and extensive public debate. In the second stage, the work was done from October to December 2004 by the Code Group, a new committee appointed by the Government, composed mainly of the same members who made up the previous working group. Its task was to make the necessary changes to the original code proposal, based on the views expressed in the comments received and from the public debate, and to present a final corporate governance code that could be applied sometime in 2005.

The Code Group was composed of Erik Åsbrink, chairman, Rune Brandinger, Claes Dahlbäck, Karin Forseke, Lars-Erik Forsgårdh, Eva Halvarsson, Arne Mårtensson, Marianne Nivert, Lars Otterbeck, Henrik Paulsson, Bengt Rydén and Patrik Tigerschiöld. Rolf Skog, Lars Thalén and Per Thorell participated in the Group as experts. Secretary of the Group was Per Lekvall and Björn Kristiansson was assistant secretary.

The bodies and organisations in the business community that, together with the central government, were the primary sponsors are FAR (the institute for the accountancy profession in Sweden), the Swedish Investment Fund Association (FondbolagensFörening), the Swedish Industry and Commerce Stock Exchange Committee (Näringslivets Börskommitté), the Stockholm Stock Exchange (Stockholmsbörsen), the Stockholm Chamber of Commerce (Stockholms Handelskammare), the Swedish Bankers' Association (Svenska Bankföreningen), the Swedish Securities Dealers Association (Svenska Fondhandlareföreningen), the Confederation of Swedish Enterprise (Svenskt Näringsliv), the Swedish Shareholders' Association (Sveriges Aktiesparares Riksförbund) and the Swedish Insurance Federation (Sveriges Försäkringsförbund).

Stockholm, December 16, 2004

Erik Åsbrink
Chairman of the Code Group

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I. Introduction

Corporate governance deals with the management of companies with a view to meeting the owners' required return on invested capital and thus it contributes to economic growth and efficiency.

In the past few decades corporate governance has evolved rapidly. As a result, many countries have introduced more or less voluntary compilations of rules, or codes, of corporate governance. International bodies such as the OECD and the EU have also drawn up guidelines for corporate governance. With the introduction of this Code, Sweden will have an equivalent body of rules.

1 A Swedish Code of Corporate Governance

Sweden has not had a comprehensive code until now, but that does not imply a lack of regulations and guidelines in this area. The Swedish Companies Act forms the basis of Swedish corporate governance. After revision and updating in the past decade, this act regulates several matters that in other countries are dealt with in codes and similar regulatory regimes. Since the Swedish Shareholders' Association published Sweden's first ownership policy in 1993, the majority of larger Swedish institutional owners have drawn up their own guidelines on how the ownership roles should be exercised. The self-regulating bodies in the business community have continued to incorporate a number of regulations on corporate governance into their regulatory systems. In 2003 the Swedish Academy of Directors issued its Guidelines for Good Board Practice, the first comprehensive description of good practice for boards of directors of Swedish companies.

Thus the current introduction of a Swedish code of corporate governance is not due to insufficient regulation. However, the Commission on Business Confidence and many in the business community share the opinion that there is a need for a more comprehensive compilation of what constitutes good Swedish practice in corporate

governance, starting from existing regulations and custom, but also improving on current practice in some respects.

1.1 The Code's Aim and Its Basic Principles

The general aim of the Code is to help improve corporate governance in Swedish companies. Even though the Code is directed primarily at stock market companies, sound corporate governance in these companies will serve as an example and a model for other types of companies. In the opinion of the Code Group this, in turn, is likely to improve efficiency and competitiveness in the business sector. It is also likely to bolster confidence in the Swedish capital market and the confidence of Swedish society generally in the way in which business functions.

A second aim of the Code is to enhance understanding and confidence in Swedish corporate governance on the part of foreign investors and other actors in the international capital markets, with a view to promoting the Swedish business sector's access to foreign risk capital on favourable terms.

Some key principles underlying the Code Group's work developing the Code have been:

- to create good conditions for shareholders to exercise the ownership role actively and responsibly,
- to create a sound balance of power between the owners, the board of directors and the executive management to enable shareholders to assert their interests vis-à-vis company management,
- to create a clear division of roles and responsibilities between the various governing and supervisory bodies,
- to uphold in practice the principle of equal treatment of shareholders as found in the Swedish Companies Act, and
- to create as much transparency as possible towards shareholders, the capital market and society in general.

1.2 Target Group

Corporate governance issues are most important in companies with broad public ownership. The Code is therefore aimed primarily

at stock market companies, that is, companies listed on a stock exchange or other authorised marketplace. However, for the most part, other types of companies with a diverse ownership or public interest – for example, other listed companies, co-operatives, state- and municipally owned companies and mutual insurance companies – as well as many privately owned companies, especially those preparing to go public, should also be able to put these rules into practice.

Good corporate governance is important in all stock market companies irrespective of their size. However, an ambitious regulatory regime may be too demanding for smaller companies to implement in its entirety. Thus the aim has been to provide enough flexibility for simplification where warranted without lowering the goal of creating an internationally respected code for the larger listed companies. Moreover, under the principle of comply or explain (see text that follows), it should also be acceptable for smaller companies to report a larger number of departures from the rules than do larger companies.

The Code Group's premise is that to begin with, companies listed on the Stockholm Stock Exchange should be obliged to apply the Code in the near future. There may be reasons for considering a step-by-step implementation, beginning with the largest and most qualified companies. The Group recommends as a first step introducing the Code in companies listed on the A-list and in the larger companies listed on the O-list. After a few years of experience gained applying the Code, coverage should be broadened to include all companies listed on the stock exchange. There are advantages to proceeding in this manner. The experience gained in the practical application of the Code can form the basis of possible modifications in connection with the Code's extension to more firms. Furthermore, the larger companies will develop systems and routines for applying the Code in a cost-effective manner. Smaller companies can then make use of any relevant parts of such systems and routines. The larger stock market companies will thus bear much of the initial costs of establishing appropriate systems and routines for applying the Code.

Implementing the Code is also recommended for companies listed on stock markets other than the Stockholm Stock Exchange as well as for many unlisted companies. The Code Group is convinced that application of the Code will come to be viewed as a sign of quality that an increasing number of marketplaces and companies will consider important to acquire.

For a company listed on stock exchanges or marketplaces in several countries, its legal domicile should decide which country's code it is to follow. The Swedish Code is thus intended for Swedish limited liability companies. If a Swedish company, because it is listed on a foreign stock exchange having mandatory rules that contravene the Swedish Code, is obliged to depart from certain rules in the Swedish Code, this obligation should generally constitute a valid reason for a departure under the principle of comply or explain.

1.3 Comply or Explain

The Code is intended to form part of self-regulation in the Swedish business sector. It is based on the principle "comply or explain", which the majority of foreign codes follow. Under this principle a company following the Code may depart from individual rules; however, in that event, it must provide an explanation stating the reasons for each departure reported. Thus applying the Code does not mean that every rule must always be observed and departing from one or more individual rules does not constitute a breach of the Code. Rather, in some instances deviating from a rule that is not suitable for an individual company may signify good corporate governance. The reason for the deviation is what is important.

With this principle, the Code's goals could be set higher than would have been possible had the rules been compulsory. With the issuance of obligatory rules, requirements must be kept at the level at which every company can reasonably be expected to comply at all times, a sort of lowest common denominator that suits everyone. Instead, with the principle of comply or explain, requirements can be set at a level expected to lead to good corporate governance while sufficient flexibility is created to take differences between companies into account. Consequently the Code provides a picture of what may generally be considered to constitute good corporate governance, even though individual companies may have reason to depart from certain rules.

One important question is what requirements should be established for explaining the reasons for any departures and who is to decide whether or not these requirements have been met. The Code contains no rules on how departures are to be explained. The Code Group's position is that it is a matter for the board of directors

in individual companies to decide. However, in some instances, it may be difficult to issue a well-founded statement explaining the reasons for a departure. For example, the shareholders' meeting could make decisions that depart from the rules of the Code without giving any reasons for these departures to the board of directors. In such instances it should be considered sufficient for the board of directors to refer to the decision of the shareholders' meeting in the corporate governance report without specifying a reason.

The Code Group is not proposing that any particular authority pass judgment on the acceptability of reasons for departing from a rule. In the case of stock market companies, it is assumed that the market, in the form of investors and other actors, will ultimately decide whether or not an explanation is acceptable. Companies that depart from the rules in the Code without giving any reasonable explanation for the divergence risk suffering a loss of confidence on the part of the capital markets, which may then have a negative impact on the company's value. For other types of companies, it is chiefly the owners' responsibility to judge the reasons for reported departures.

1.4 Form and Content of the Code

The Code deals with the decision-making system used by the shareholders to govern the company, both directly and indirectly. This is expressed in a number of rules on the organisation and working methods of individual company governance bodies and the interaction between these bodies. In addition there are guidelines on reporting to shareholders, the capital market and the general public.

The Code's rules represent an addition mainly to the provisions in the Swedish Companies Act on a company's organisation, but also to the relatively extensive self-regulation that exists in the area of corporate governance. Such self-regulation is found in the listing requirements and listing agreements of the Stockholm Stock Exchange, Nordic Growth Market NGM and AktieTorget; the rules of the Swedish Industry and Commerce Stock Exchange Committee; statements by the Securities Council; and FAR's rules and regulations.

The provisions of the Swedish Companies Act are not repeated in the Code's rules, but the comments to provisions in the Code do refer to them to facilitate reader comprehension where appropriate.

Likewise, an aim in writing the Code has been to avoid an overlap with self-regulation. Here, however, certain exceptions have been made, primarily to take into account EU recommendations recently issued in this area, for example, the criteria for directors' independence and certain remuneration issues. Furthermore, the Code, as previously mentioned, is also intended for other types of companies in addition to those covered by the rules for stock market companies.

The Code does not deal with issues concerning the audit function and the way in which the stock market works. Nor does it deal with relations with customers, employees or the general public. These matters have not been considered part of corporate governance. The rules in the Code are designed to provide guidance to companies. This means that in most cases, rules are intended for the board of directors, but certain rules are meant for the shareholders' meeting, the auditors or the managing director. Thus under the Code, these bodies are assumed to be part of the company.

Two types of text are used in the Code:

- The rules in the Code are shown in normal type. Departures from the rules are to be reported and explained under the principle, comply or explain. To avoid introducing uncertainty about the requirements for observing individual rules, "is to" has been used throughout. However, this does not mean that the rule is compulsory. As previously stated, it is possible to deviate from individual rules without breaching the Code as a whole.
- The introductory text of main sections and some sub-sections is shown in italics. The aim of this introductory text is to provide a clear statement of the fundamental approach forming the basis for the rules that follow. It does not constitute rules and there is no requirement to report or explain departures from what is stated there.

In addition there are comments on certain rules in the footnotes. Their aim is to explain, when necessary, the intended meaning of the rule or to put the rule in a context that makes it easier to understand. Such text is not part of the rule per se, so companies do not need to act on this text in any particular way in the event of any departures.

2 Swedish Corporate Governance in an International Context

In its main features, the Swedish model of corporate governance is fundamentally the same as the models of corporate governance applied in most industrialised countries. At the same time, owing in part to different ownership structures and traditions and to legislation and other regulations in the area, there are certain distinctive features that have to be taken into account in drawing up a Swedish code of corporate governance. Some of these distinctive features are reported in point form below, principally in relation to the Anglo-American model that has come to dominate international developments in the area.

- The ownership structure of the companies listed on the Swedish stock market differs substantially from that in such countries as the United Kingdom and the United States. While the majority of listed companies in these countries present a very dispersed ownership picture, it is common for one or a few major owners to dominate ownership in Swedish listed companies (as in most continental European countries). These owners often actively exercise their ownership role and take a particular responsibility for the company in various ways such as taking part in the board of directors.
- The Swedish Companies Act provides for a hierarchical governance structure in which senior governance bodies can issue directives to subordinate bodies or even take over their decision-making authority. A Swedish shareholders' meeting is sovereign in deciding all the company's affairs, including, where appropriate, issuing express instructions to the board of directors and the managing director on the company's management. However, such directives are rarely issued in listed companies.
- As a rule, each shareholder in attendance at the shareholders' meeting has the right to vote for all shares owned. The articles of association may provide that each shareholder may only vote for a certain number of shares, but in practice, such restrictions on voting rights are very uncommon. In addition the Swedish Companies Act permits shares with differentiated voting rights. However, the maximum ratio is 1:10. About half of the Swedish stock market companies currently have such differentiation in

voting rights. Swedish limited liability companies do not have the right to issue nonvoting shares.

- The decisions of the shareholders' meeting are generally taken with a simple majority of the votes cast. However, to protect minority shareholders, especially shareholders with reduced voting rights, requirements have been drawn up for qualified majorities of both votes and capital for major decisions. In addition there is a general rule for the protection of minority shareholders prescribing that the shareholders' meeting may not make a decision that might give undue advantage to some shareholders at the expense of the company or other shareholders.
- Under the law, the shareholders' meeting elects the company's board of directors and decides on discharge of liability for members of the board and the managing director. The meeting's decision on the appointment of the board of directors is therefore normally prepared under a process controlled by the owners.
- Under Swedish law, the company's auditors are also appointed by the shareholders' meeting. The auditor's task is not only to examine the company's annual accounts and accounting practices, but also to review the management of the company by the board of directors and the managing director. Thus one important aim of the auditors is to satisfy the owners' requirements to control the board of directors and the managing director. Today the auditors are also considered to have the aim of protecting the interests of other stakeholders in the company, such as employees, creditors and capital market actors.
- The Swedish model's basic structure for corporate governance by the owners lies somewhere between the Anglo- American one-tier model and the continental European twotier model. A Swedish limited liability company must have a board of directors and a managing director. The board is responsible for the company's organisation and the management of the company's affairs. The extensive decision-making authority thus assigned the board is limited primarily by the exclusive decision-making powers of the shareholders' meeting in certain matters and the meeting's right to issue instructions to the board.
- One distinctive feature when compared with the Anglo-American model is the structure of the board of directors. The Swe-

dish Companies Act requires a certain degree of separation in the exercise of the executive and management authorities. Thus in public limited liability companies¹, the same person cannot be the managing director and chair the board. Further in most listed companies in Sweden, no members of the board come from the company's senior management other than the managing director. Thus, other than the managing director and the employee representatives on the board (see text that follows), the board of directors in a Swedish company listed on the stock exchange is normally composed exclusively of non-executive directors. Persons with links to major shareholders usually constitute a majority on the board and only a few directors are independent of the major shareholders.

- Employees have the right to representation on the board of Swedish companies. In a few words, in companies with at least 25 employees, employees have the right to appoint two representatives to the board of directors and two deputy members, while in companies with activities in several lines of business and a minimum of 1,000 employees, they have the right to appoint three representatives and two deputies. However, employee representatives may never constitute a majority on the board.
- A managing director appointed by the board of directors is mandatory in limited liability companies. The managing director is responsible for the company's day-to-day management but, unlike the two-tier model, the Swedish managing director is subordinate to the board. The managing director is obliged, within the bounds defined by the law and the articles of association of the company, to follow instructions from the board on how routine management measures are to be handled or decided. The board may also decide on matters that are part of the day-to-day management but must not intervene in the day-to-day operations to such an extent that the managing director in reality may no longer be considered to have that position. The managing director is also obliged to follow any directives that the shareholders' meeting might issue.

¹ The Swedish Companies Act distinguishes between private and public limited liability companies, the main difference being that the latter can promote the sale of its shares to broad circles of potential investors and list the shares for trading on a stock exchange or other organised marketplace, steps that a private company is not allowed to take. Hence all listed companies are by definition public limited liability companies.

II. The Ownership Role and Responsibility

A dynamic and competitive business sector requires a well-functioning capital market through which to channel savings in the form of loan capital and risk capital to companies for investment.

Owners that take responsibility for the firm's development are an important element of an efficient market economy. Shareholders provide risk capital to the economy, but they also contribute to the efficiency and innovative capacity of individual firms and the business sector generally by exercising influence via the shareholders' meeting as well as by buying and selling shares.

A dynamic business sector requires a diverse ownership with different investment aims, time horizons and risk propensity. A wellfunctioning market for controlling shareholdings and the acquisition of companies also promotes a dynamic business sector.

Shareholders with large holdings in stock market companies should make use of the opportunity provided by the shareholders' meeting to exercise influence in the company, among other things, through the election of the company's board of directors, and should have a well thought-out policy on how to exercise the ownership role in the company. Shareholders' active participation in the shareholders' meeting promotes a sound balance of power between owners, the board of directors and senior management.

Shareholders with large holdings in stock market companies have a special responsibility not to abuse their power to the detriment of the company or other shareholders. Shareholders with a minority interest have a responsibility not to abuse their minority rights to the detriment of the company or other shareholders.

Institutional owners, such as pension funds, life insurance companies, mutual funds, investment companies and others, should make their ownership policy public and so inform investors of their

investment philosophy and the principles followed in exercising the voting rights attached to the shares. In particular, information should be made available showing how the underlying interests of investors are looked after. Where appropriate, institutional owners should also provide information about potential conflicts of interest that might affect the exercise of the ownership function. Investors should have easy access to information on how the voting rights have been exercised in each instance as well as the underlying considerations.

III. Rules for Corporate Governance²

1 The Shareholders' Meeting

Shareholders' influence in the company is exercised at the shareholders' meeting, which is the company's highest decisionmaking body. To create the best possible conditions for the active exercise of the ownership role, the shareholders' meeting should be conducted in such a manner that as high a percentage as possible of the total number of shares and votes can be represented at the meeting and that active participation on the part of current shareholders in the discussions and decision making is facilitated.

1.1 Notice of Shareholders' Meeting

- 1.1.1 As soon as the board of directors has decided to hold an extraordinary shareholders' meeting, but no later than the time of the third quarter report, the company is to announce the time and location of the meeting. The information is to be posted to the company's web site at the same time that it is announced.
- 1.1.2 Before issuing a notice of an annual general meeting, the company is to provide timely information on its web site on the shareholders' right to have a matter considered at the meeting and the time when such a request must reach the company in order to guarantee its inclusion in the notice of meeting. When possible, similar procedures are to be followed before an extraordinary shareholders' meeting.

² The rules in the Code are shown in normal type. The aim of the introductory text to individual sections shown in italics is to provide a clear statement of the fundamental approach forming the basis for the rules that follow. The aim of the footnotes is to comment on or to explain, when necessary, the intended meaning of the rule or to put it in a context that makes it easier to understand.

- 1.1.3 Shareholders are to be given the opportunity to register to attend the shareholders' meeting in several ways, among them registration by e-mail or on the company's web site.

1.2 Distance Participation

- 1.2.1 At each shareholders' meeting, the company is to provide shareholders with the option of following or participating in the meeting from another location in the country or abroad with the help of modern communications technology if it is warranted by the ownership structure and financially feasible.

1.3 Board, Management and Auditor Attendance

- 1.3.1 At shareholders' meetings, a quorum of the board is to be present. If possible, the entire board is to be present at the annual general meeting. The chair of the board of directors, the managing director and, if necessary, other company managers are to be present at the meeting. At least one of the company's auditors is to be present at the annual general meeting.
- 1.3.2 If proposals for decisions on certain items have been prepared by a committee of the board, the chair or another member of the committee is to be present at the shareholders' meeting and describe and give cause for the proposals on behalf of the board.

1.4 Conducting the Shareholders' Meeting

- 1.4.1 The company's nomination committee is to recommend a candidate to chair the annual general meeting. The recommendation is to be included in the notice of the shareholders' meeting and presented by the nomination committee at the meeting.
- 1.4.2 A shareholder, or a representative of a shareholder, who is neither a director nor an employee of the company, is to be chosen to verify the minutes of the shareholders' meeting.
- 1.4.3 The shareholders' meeting is to be conducted in Swedish and the material presented is to be in Swedish. The company is to consider whether the proceedings are to be simultaneously translated in whole or in part and whether the material presented by the company is to be translated into any other

language as warranted by the ownership structure and if financially feasible.

- 1.4.4 The chair of the shareholders' meeting is to see that the shareholders are given sufficient opportunity to exercise their statutory right to ask questions at the meeting as well as to comment on the items on the agenda, recommend changes and additions to the proposals presented, and submit new proposals in accordance with statutory provisions before the meeting comes to a decision.
- 1.4.5 The minutes from the last annual general meeting and any subsequent extraordinary shareholders' meeting are to be posted on the company's web site. It is not necessary to report the register of voters from the meeting. The protocol is also to be translated from Swedish into any other language as warranted by the ownership structure.

2 Appointment of the Board and Auditors

The decisions of the shareholders' meeting on the appointment of the board of directors and auditors should be prepared by a structured and transparent process governed by the shareholders. It should provide all shareholders with the opportunity to express their views on proposals and present proposals on the issues at hand. It should also provide a good basis for making well-founded decisions.

2.1 Nomination Committee

The nomination committee is a body of the shareholders' meeting that prepares the decisions on appointments to be taken by shareholders at the shareholders' meeting. The committee's aim is to provide a sound basis for the meetings' consideration of these matters.

- 2.1.1 The company is to have a nomination committee that represents the company's shareholders. The shareholders' meeting is to appoint members of the nomination committee or to specify how they are to be appointed. The decision is to include procedures for replacing members of the nomination committee who resign before its work is concluded, if necessary.

If members of the nomination committee are not appointed

by the shareholders' meeting, the meeting is to decide on the criteria to be used in appointing the chair and members of the nomination committee.

- 2.1.2 The nomination committee is to have at least three members. The majority of the members of the nomination committee are not to be members of the board of directors. The managing director or other company managers are not to be members of the nomination committee. The chair of the board of directors or another board member is not to chair the nomination committee.³
- 2.1.3 The company is to announce the names of members of the nomination committee at least six months before the annual general meeting. If a member represents a particular owner, that owner's name is to be stated. The replacement of a member of the nomination committee is to be made public and the corresponding information about the new member is to be provided. The information is to be found on the company's web site, which is also to specify how shareholders may submit recommendations to the nomination committee.

2.2 Appointment of the Board of Directors

- 2.2.1 The nomination committee is to make recommendations for the chair and other members of the board and recommendations on the division of board fees among the chair and other directors and on remuneration for committee work, if any.
- 2.2.2 As the basis for its recommendations, the nomination committee is to:
- assess the extent to which the current board meets the demands that will be made of the board as a consequence of the company's current position and future direction, among other things, by studying the result of the evaluation made of the board,
 - establish requirements profiles for the new member or members who, according to this assessment, should be recruited, and

³ The nomination committee should not include any members who represent any of the company's competitors.

- execute a systematic procedure for the recruitment of directors, with due consideration for shareholders' recommendations.⁴

2.2.3 The nomination committee's recommendations are to be presented in the notice of the shareholders' meeting and on the company's web site. The following information for persons nominated for election or re-election to the board is to be posted on the company's web site in connection with the issuance of the notice of the shareholders' meeting:

- age and principal education and work experience,
- any work performed for the company and significant professional commitments outside the company,
- his or her own holdings of shares and other financial instruments in the company or such holdings by related natural or legal persons,
- if, according to the nomination committee, the board member is considered to be independent of the company and its senior management, as well as of major shareholders in the company,
- on re-election, the year that the member was first elected to the board, and
- other information that may be important to shareholders in assessing the proposed member's competence and independence.

A report on how the nomination committee has conducted its work is to be posted on the company's web site.

2.2.4 At the shareholders' meeting, the nomination committee is to present and give reasons for its recommendations. It is to specify its reasons if its recommendations do not include any new nominees. In addition, the nomination committee is to submit a report on how it has conducted its work.

⁴ In light of the information that may need to be given to members of the nomination committee, the company may have reason to reconsider its confidentiality agreements aimed at eliminating the risk that such information is divulged to owners on a selective basis.

- 2.2.5 Persons recommended for election to the board are to be present at the meeting, if possible, so that they can introduce themselves and answer questions from shareholders.
- 2.2.6 The shareholders' meeting is to decide on directors' fees and all other remuneration for board work and the allocation to the chair and other members of the board and remuneration for committee work, if any.
- 2.2.7 Directors are not to participate in share or share-price incentive schemes aimed at company management or other employees. If such a programme is intended for the board alone, the shareholders' meeting is to decide the programme. The decision is to specify the maximum number of instruments that may be issued, the main terms of the allocation, the main terms and principles to be observed when estimating the value of the instrument and the latest date that the instrument can be issued or transferred to the board member.

Even though the managing director is a member of the board, he or she may participate in incentive schemes intended for management and employees.

2.3 Appointment of Auditors

- 2.3.1 Recommendations on the appointment of auditors are to be made by the company's nomination committee or a nomination committee appointed especially for that purpose. When a separate nomination committee is appointed, the regulations in 2.1 and this section apply.
- 2.3.2 In connection with the issuance of the notice of the shareholders' meeting, information that may be of importance to shareholders in assessing the competence and independence of the proposed auditors is to be posted on the company's web site. The information is to show what services other than auditing were provided by the proposed auditor to the company over the past three years and, in the event of reelection, the year that the auditor was first appointed and the length of the engagement. A report on how the nomination committee has conducted its work is to be posted on the company's web site.

- 2.3.4 At the shareholders' meeting, the nomination committee is to present and give reasons for its recommendations and submit a report on how it has conducted its work.
- 2.3.5 The proposed auditor is to be present at the meeting to be introduced and answer questions from the shareholders.

3 The Board of Directors

3.1 Tasks

The principal task of the board of directors is to manage the company's affairs in such a way as to satisfy the owners that their interests in a good long-term return on capital are being met in the best possible way.

- 3.1.1 To meet its obligations to the company's owners, the board of directors is to pay particular attention to:
- establishing the overall goals for the company and deciding the company's strategy for achieving these goals,
 - evaluate the company's operative management on an ongoing basis and, if necessary, appoint or dismiss the managing director,
 - ensure that there is an effective system for follow-up and control of the company's operations and financial position vis-à-vis the established goals,
 - ensure that the company's external communications are open, objective and appropriate for the target audience,
 - ensure that there is a satisfactory process for monitoring the company's compliance with laws and other regulations that apply to the company's operations, and
 - ensure that the necessary guidelines governing the company's ethical conduct are established.
- 3.1.2 The board is to ensure that there is an annual evaluation of its work and that this evaluation employs a systematic and structured process.

3.2 Size and Composition of the Board

The board should have a size and composition that enable it to embrace the various qualifications and experience needed and to meet the independence criteria required to manage the company's affairs effectively and independently. The renewal of the board should be paced with due consideration for the development of the company's operations as well as for the need for continuity in the work of the board.

- 3.2.1 With the company's operations, phase of development, and other conditions taken into consideration, the board is to have an appropriate composition, exhibiting diversity and breadth in the directors' qualifications, experience and background. An equal gender distribution on the board is to be an aim.
- 3.2.2 The board is not to exceed the size that will allow it to employ simple and effective working methods. There are to be no deputies to the directors chosen by the shareholders' meeting.
- 3.2.3 No more than one person from senior management may be a member of the board.
- 3.2.4 The majority of the directors elected by the shareholders' meeting are to be independent of the company and its management. A director is not to be considered independent if he or she:
- is the managing director, or in the preceding five years has been the managing director, of the company or associated enterprises,
 - is employed, or in the preceding three years has been employed, in the company or an associated enterprise,
 - receives significant remuneration for advice or services in addition to board work from the company or an associated enterprise or from someone in the senior management,
 - has, or in recent years has had, extensive business ties or other extensive financial dealings with the company or an associated enterprise, in his or her capacity as customer, supplier or part-owner, either personally or as part of the senior management or the board or by being a major partner in another enterprise having such a business relationship with the company,

- is, or in the past three years has been, a partner or employee of the audit firm currently or then auditing the company or an associated enterprise,
- is part of senior management in another enterprise having a director who is part of senior management in the company,
- has been a member of the board for more than twelve years, or
- is a close relative or family associate of someone in the senior management or of some other person as provided in the preceding clauses, if this person's direct or indirect dealings with the company are sufficiently extensive and important that the director is not considered independent.

An associated enterprise refers to an enterprise in which the company, directly or indirectly, holds at least 10 per cent of the shares or participation or the votes or a financial interest that gives the right to at least 10 per cent of the return of this enterprise. If the company has more than 50 per cent of the capital or votes in another enterprise, the company is considered to have indirect ownership of this enterprise's ownership in other enterprises.

The fourth point is not to apply to the customary bank-client relationships.

- 3.2.5 At least two of the directors who are independent of the company and its management are also to be independent of the company's major shareholders. A director who represents a major owner or is employed or a member of the board in a company that is a major shareholder is not considered independent.

"A major shareholder" refers to owners who directly or indirectly control 10 per cent or more of the shares or votes in the company. If one company has more than 50 per cent of the capital or votes in another company, the first company is considered to have indirect control of the second company's ownership in other companies.

- 3.2.6 Members of the board are to be appointed for one year at a time.

3.3 Directors

The director's position in relation to the company is similar to that of a trustee. This means that the director is obliged to devote the time and the care and have the competence required to look after the interests of the company and its owners in the best possible manner.

- 3.3.1 A director is not to have so many other duties that he or she is unable to devote the necessary time and care to the company's board work.
- 3.3.2 A director is to form an independent judgement on each matter considered by the board and to express the views and take the positions that follow from this judgement. A director is to request whatever supplementary information that he or she believes is necessary for the board to make well-founded decisions.
- 3.3.3 A director is obliged to acquire the familiarity with the company's operations, organisation, market, etc. needed to discharge his or her duties.
- 3.3.4 A new director is to receive the necessary introductory training about the company and any other training that the chair of the board and the director mutually consider appropriate.

3.4 The Chair of the Board of Directors

The chair has a special position in the board with explicit responsibility for seeing that the work of the board is well organised and efficiently conducted and that the board discharges its duties.

- 3.4.1 The chair of the board is to be elected at the shareholders' meeting. If the chair relinquishes his or her duties during the mandate period, the board is to elect a chair from amongst its members to serve until the end of the next shareholders' meeting.
- 3.4.2 If the nomination committee proposes that the outgoing managing director, soon after leaving that position, become the chair, the committee is to give special cause for its proposal.
- 3.4.3 If the chair of the board is employed in the company or in addition to his or her responsibilities as chair, has duties assigned by the company, these may not involve tasks that are part of the managing director's responsibilities in the day-to-

day management of the company. In such cases, the division of work between the chair and the managing director is to be clearly stated in the formal work plan of the board of directors and in the board's instruction to the managing director.

3.4.4 The chair is to ensure that the work of the board is pursued effectively and that the board discharges its duties. Specifically, the chair is to:

- organise and lead the board's work, encourage an open and constructive discussion in the board in which all the directors participate, and create the best possible conditions for the board's work,
- ensure that the board regularly updates and improves its knowledge of the company and its operations and receives any other training required to conduct the board's work effectively,
- be receptive to owners' views and communicate these views to members of the board,
- keep in regular contact with the company's managing director and function as a discussion partner and support for the managing director,
- see that the board in its work receives sufficient information and supporting data on which to base its decisions,
- after consulting with the managing director, draw up proposals for the board meeting's agenda,
- verify that the board's decisions are implemented efficiently, and
- see that the work of the board is evaluated annually and that the nomination committee is informed of the result of the evaluation.

3.5 Board Procedures

3.5.1 The board's statutory instructions in the form of its formal work plan, instruction to the managing director and reporting instruction are to be tailored to the company's circumstances and are to be so clear, detailed and functional that they can

serve as guiding documents for the board's work. At least once a year, the board is to review the relevance and currency of these instructions.

- 3.5.2 The board may establish special committees to prepare the board's decisions in specific areas and, if the board considers it appropriate, to delegate certain decision-making powers to such committees. The establishment of committees must not cause the board to lose its overall view and control of the company's business activities. Nor must the board be any less well informed. The formal work plan of the board is to specify the duties and decision-making powers that the board has delegated to the committees and indicate how the committees are to report to the board. Committees are to keep minutes of their meetings and the minutes are to be communicated to the board.
- 3.5.3 The board is to evaluate the work of the managing director on a regular basis. At least once a year, the board is to take up this matter. At that time, no one from senior management is to be present.
- 3.5.4 The board is not to take decisions on important matters that have not been placed on the agenda, unless the board unanimously decides to do so.
- 3.5.5 The board is to be assisted by a board secretary who is not a member of the board.
- 3.5.6 The minutes of the board are to be a clear representation of the matters discussed, the supporting material available for each item and the content of the decisions taken. The minutes are to be sent to directors as soon as possible after the board meeting.

3.6 Financial Reporting

The board of directors is responsible for seeing that the company's financial reports have been prepared in accordance with the law, the relevant accounting standards and other requirements for listed companies.

- 3.6.1 The annual report and interim reports are to make clear those parts that are formal financial statements, the regulatory regime on which they are based, and those parts of the an-

nual report or interim report that are audited or reviewed by the company's auditors.⁵

- 3.6.2 The board of directors and the managing director, immediately before signing the annual report, are to certify that to the best of their knowledge, the annual accounts have been prepared in accordance with good accounting practices for a stock market company and that the information presented is consistent with the actual conditions and that nothing of material value has been omitted that would affect the picture of the company presented in the annual report.
- 3.6.3 The company's six- or nine-month report is to be reviewed by the auditors.

3.7 Internal Control and Internal Auditing

The board is responsible for the company's internal control, which has the general aim of protecting the shareholders' investment and the company's assets.

- 3.7.1 The board is to ensure that the company has a sound system of internal controls and keep itself informed of and assess how well it functions.
- 3.7.2 The board is to submit an annual report on how that part of internal control dealing with financial reporting is organised and how well it has functioned during the most recent financial year. The report is to be reviewed by the company's auditors.
- 3.7.3 The board in companies that do not have a special internal audit function is annually to evaluate the need of such a function and explain the position that it has taken in its report on internal control.

3.8 Accounting and Auditing Issues

The board is responsible for seeing that the company has a formal and transparent system that ensures that the principles established for financial reporting and internal control are observed and that appropriate relations with the company's auditors are maintained.

⁵ Under IAS 1, financial statements refer to the income statement, the balance sheet, the statement of changes in equity, the cash flow statement and a statement of accounting principles and notes.

3.8.1 The board is to document and present information on the manner in which the board ensures the quality of the financial reports and how it communicates with the company's auditors.

3.8.2 The board is to establish an audit committee consisting of at least three directors. The majority of the audit committee members are to be independent of the company and senior management. At least one member of the committee is to be independent of the company's major shareholders. A board member who is part of senior management may not be a member of the committee.

In companies with smaller boards, the entire board may perform the audit committee's tasks, provided that a director who is part of the senior management does not participate in the work.

3.8.3 The audit committee is to:

- be responsible for the preparation of the board's work to ensure the quality of the company's financial statements,⁶
- meet regularly with the company's auditors to keep informed of the aims and scope of the audit work and to discuss co-ordination between external and internal audit and views on the company's risks,
- establish guidelines on other services in addition to audit that the company is allowed to procure from the company's auditors,
- evaluate the audit work and inform the company's nomination committee, or where appropriate, the separate nomination committee appointed to propose auditors, of the result of the evaluation, and
- assist the company's nomination committee in preparing nominations for auditors and recommendations on audit fees.

3.8.4 At least once a year, the board is to meet the company's auditors without the managing director or any other company executive being present.

⁶ To ensure the quality of the financial statements, the committee normally has to consider all critical accounting questions and the financial reports presented by the company. The committee is presumed to consider matters such as internal control, regulatory compliance, material uncertainty in reported values, uncorrected errors, post-statement events, possible improprieties and other circumstances that may affect the quality of the financial statement information.

4 Company Management

4.1 The Managing Director's Duties

Whether or not the managing director is a member of the board, he or she has a special role in the work of the board. As part of this role, the managing director reports to the board on the company's progress, submits reports and recommendations on matters prepared by company management and provides the board with information on which it bases its work.

- 4.1.1 The managing director is to see that the board gets as objective, full and relevant an information basis as it requires to make well-founded decisions and that the board is kept informed of the progress of the company's business operations between board meetings.
- 4.1.2 The board is to approve any significant professional commitments of the managing director outside the company.

4.2 Senior Management Remuneration

The board is responsible for seeing that the company has a formal process, which is transparent for all board members, for establishing the company's policy for remuneration and other terms of employment for senior management and for deciding the managing director's remuneration and other terms of employment.

- 4.2.1 The board is to establish a remuneration committee with the task of preparing proposals on remuneration and other terms of employment for senior management. The chair of the board may chair the remuneration committee. The other members of the committee are to be independent of the company and senior management. In companies with smaller boards, the entire board may perform the remuneration committee's tasks, provided that a director who is also part of the senior management does not participate in the work.
- 4.2.2 The board is to present a proposal for the company's policy on remuneration and other terms of employment for senior management to the annual general meeting for its approval. The proposal is to be posted on the company's web site in

connection with the notice of the shareholders' meeting. The policy is to include:

- the relative importance of fixed and variable components of the remuneration and the linkage between performance and remuneration,
- the principal terms of bonus and incentive schemes,
- the principal terms of non-monetary benefits, pension, notice of termination and severance pay, and
- the members of senior management covered by the terms.

The proposal is to state whether the terms recommended differ significantly from the policy approved earlier by the shareholders' meeting and how matters of senior management remuneration are prepared and decided by the board.

- 4.2.3 The shareholders' meeting is to decide all share and share-price incentive schemes for senior management. The decision is to specify the maximum number of instruments that may be issued, the main terms of the allocation, the main terms and principles to be observed when estimating the value of the instrument and the latest date on which the instrument can be issued or transferred to senior management.

5 Information on Corporate Governance

5.1 Corporate Governance Report

- 5.1.1 A special report on corporate governance is to be attached to the company's annual report. The report is to include a statement on whether or not the company's auditors have reviewed it.⁷
- 5.1.2 In the corporate governance report, the company is to state that it is applying the Code and give a brief description of how this has been done in the most recent financial year.

⁷ The report may be included in the printed annual report or constitute a separate report but it is not part of the formal financial statements.

The company is to indicate where it has departed from the rules in the Code. The reasons for each departure are to be clearly explained.

- 5.1.3 The corporate governance report is to present information on the manner in which the board ensures the quality of the financial reports and communicates with the company's auditors in accordance with 3.8.1.
- 5.1.4 The corporate governance report is also to provide the following information, if it is not included in the annual report:
- a statement explaining the procedures leading to the appointment of the board of directors and auditors,
 - the composition of the company's nomination committee and where appropriate, a separate nomination committee appointed to propose auditors. If a member of such a committee has represented a particular owner, that owner's name is to be stated,
 - for each member of the board, the information to be provided in accordance with the points listed in 2.2.3,
 - for auditors, the information to be provided in accordance with the first and second sentences of 2.3.3,
 - the division of work among directors and a statement on how the work of the board was conducted during the most recent financial year, including the number of board meetings and each member's attendance at board meetings,
 - the composition, tasks and decision-making authority of board committees, if any, and each member's attendance at committee meetings,
 - for the managing director:
 - age and principal education and work experience,
 - significant professional commitments outside the company,
 - his or her own holdings of shares and other financial instruments in the company or those holdings by related natural or legal persons,

- material shareholdings and part ownership in enterprises with which the company has business ties,
- the policy on remuneration and other terms of employment for senior management approved at the most recent shareholders' meeting and, in the event of significant differences from the preceding year's terms, a statement of what these differences are and the procedures followed by the board in preparing matters of remuneration for senior management, and
- outstanding share and share-price incentive schemes for the board and senior management.

5.2 Report on Internal Controls

- 5.2.1 The board's report on internal controls and the auditors' review of this report is to be appended to the company's annual report in accordance with 3.7.2.⁸

5.3 Information on the Company's Web Site

- 5.3.1 The company is to have a special section on its web site for corporate governance matters. This section is to provide current information on the state of corporate governance in the company that is included in the corporate governance report, together with other information as required under the Code.⁹

⁸ This report may also be included in the printed annual report or constitute a separate report but it is not part of the formal financial statements.

⁹ Companies that apply the Code should see that the information on corporate governance is easily accessible to shareholders and other interested parties by assembling this information in one place on the company's web site. It is important to keep this information reasonably current. Among other things, this means that much of the information called for under the requirements for the corporate governance report in 5.1 should be made available on the company's web site before the corporate governance report is published in conjunction with the annual report. The information on the web site should be updated at least after every shareholders' meeting and in connection with the issuance of the interim reports.