

KOLLEGIET
FÖR SVENSK BOLAGSSTYRNING

The Swedish Corporate Governance Board

Annual Report 2006

Abbreviated Version



Contents

This is an abbreviated version of the Swedish edition, including the Board's report of its first year of activities and the results of the studies of the Code application commissioned by the Board. The Swedish edition also contains articles by external authors, dealing with corporate governance development in general in Sweden and the other Nordic countries as well as a report (in English) on the 2005 review of the UK Combined Code.

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Foreword

The Swedish Code of Corporate Governance was presented in revised form in December 2004. The Code became compulsory for companies listed on the Stockholm Stock Exchange on 1 July 2005.

The Swedish Corporate Governance Board was set up in 2005 as a vital link in the chain of self-regulation within corporate Sweden. The Board reports to the Association for Good Practice on the Securities Market, which comprises a number of large organizations within Swedish business and industry.

Transparency is a key component of good corporate governance, as are efficiency and loyalty in the boardroom. The work and deliberations of the Board must be characterized by openness, and the working methods must promote open and unbiased discussion, both internally and in its consultations with those who work with the code at first hand.

The first year of corporate governance using the Swedish Code of Corporate Governance is almost at an end and in this report, the Board aims to provide a basis for learning and discussion about Swedish corporate governance. Our ambition is to provide annual information, evaluations and assessments of the development of corporate governance in Sweden, along with a brief survey of developments in other countries and sectors.

In the chapter “The First Year – What Have We Learnt?” we offer a preliminary assessment based on the experience gained from the first year of corporate governance. After a deeper analysis and, we hope, lively public discussion, we will present our conclusions and decisions during autumn 2006. In the chapter “The Work of the Board”, we present an overview of the work of the Board since its formation in spring 2005.

The articles in the section “Application of the Code” are written by individual people, and the content is therefore the responsibility of each respective author.

On behalf of the whole Board, I would like to express my hope that this document will provide a basis for continued constructive debate on the Swedish Code of Corporate Governance and other corporate governance issues.

Stockholm, June 2006

Hans Dalborg
Chair of the Board

During the year, the Board comprised the following members:

Chair	Hans Dalborg	Co-opted Member	Jukka Ruuska
Deputy Chair	Lars Otterbeck		
Ordinary Members	Lars-Erik Forsgårdh	Secretary	Per Lekvall
	Kerstin Hessius		
	Leif Lindberg	Adviser – Communications	Lars Thalén
	Anders Malmeby		
	Marianne Nilsson		
	Marianne Nivert		
	Michael Treschow		
	Anders Ullberg		

The first year – what have we learnt?

Sweden need a code of good corporate governance in order to defend the competitiveness of Swedish listed companies and Swedish listings on the international capital market, to reinforce Swedish confidence in how Swedish listed companies are run and to avoid unnecessary legislation by exercising competent and appropriate self regulation.

The Swedish Code of Corporate Governance is based on Swedish legislation and Swedish ownership conditions, but must be adapted to international conditions, (primarily Nordic and European), as far as possible. It should be easy to use by virtue of its simplicity, clarity and avoidance of unnecessary detail. Corporate governance must be more a question of quality than of quantity.

In this report, the Swedish Corporate Governance Board presents a number of general observations regarding application of the Code so far and some conclusions in anticipation of future reviews of the Code. We also highlight some areas where we feel that certain modifications of the Code or its application might already prove beneficial.

General Observations

The general view of the Board is that the Swedish Code of Corporate Governance has been applied sensibly and that its use has spread well beyond the sectors in which it is compulsory. The first year has shown that there is both room for improvement in the field of corporate governance and a need to defend the Nordic corporate governance model internationally.

Content and form

Codification means that less time will need to be spent on form and more can be devoted to content, i.e. discussion of strategies and business issues. When the rules exist in written form, the spoken word can be devoted to business, whether in the internal work of the company, in the boardroom or at the annual general meeting. This has been seen already during the first year, e.g. less time has been spent on points of order at annual general meetings. Reports on the work of the board, the audit and decisions

on remunerations may result in longer AGMs, but this does not necessarily mean that business-critical decisions receive less focus.

Target group

Application of the Code was limited to the largest companies listed on the Stockholm Stock Exchange – seventy seven companies initially, with eight more added in May 2006. This seems to have been a wise starting point. The companies covered by the Code have applied it, and the assessments made by other actors show that the effects of the Code have spread to other listed companies and unlisted companies on a significant scale from the very beginning.

Comply or explain

The small number of explanations found within the framework of “comply or explain” shows that the Code has not been impossible to apply or comply with in practice. Companies, the stock market and the media have shown the maturity required by a “comply or explain” system. Explanations have usually been detailed and well founded, and in principle been neither misinterpreted nor abused.

The only item in the text of the Code that was impossible or inappropriate to comply with was the section on internal controls regarding financial reporting. When the transition period proved too short for companies and auditors, the Board provided a general provisional solution.

The role and responsibility of owners

The discipline of corporate governance has its origins in the fact that more and more listed companies have an increasingly widespread ownership, both nationally and internationally. The aim is to ensure that the shared interests of the owners are reflected in the way the company is run. Good corporate governance is a prerequisite for a competitive capital market.

The Swedish Code emphasizes that large shareholders should make use of their possibilities to exert influence on listed companies at AGMs. Most institutional owners do this actively, whereas the opposite has been true of others. International institutions often use proxies with



fixed mandates and a simple “No” on their ballot papers. On issues with a strong protection of minority interests, requiring up to 90% support at the AGM, this can create problems. Meetings can be unable to make decisions on certain issues, and in certain cases, it is debatable whether this would be in the owners’ interest. The situation is fundamentally an expression of something positive: More owners are participating at AGMs and voting. However, the tendencies apparent at AGMs in 2006 ought to lead to a broad debate and some soul searching among certain actors.

Some of the questions that have been brought into focus are: How should proposals be communicated to major shareholders in order to gain support before the annual general meeting? How can advisers learn enough about the Swedish Companies Act to be able to offer advice in the interests of their clients? Should delegates accept situations whereby they attend an annual general meeting with a set of fixed yes or no ballot papers, and if so, how should they behave so as not to spread confusion? How should the annual general meeting be led and run with documentation of yes and no votes? Should articles of association and voting rules be adjusted to meet these circumstances? Can Swedish legislation continue in the long term to have rules on matters which do not exist in other markets, such as annual general meeting decisions about discharging boards from liability?

A General Review

After just one year, it is too early to judge whether the Swedish Code of Corporate Governance fulfils its purposes and whether it meets the criteria for a good code originally set out. The Board has assumed that a couple of years are needed at large corporations before a general review of the Code can be carried out and presented in the light of experience, changes in the business environment and the application of the Code in all listed companies.

In December 2005, the Board held a meeting with around 50 representatives of companies covered by the Code. Based on the experiences of these representatives’ work in applying the code in large companies, along with the assessments presented in this report, the Board can already propose a number of guidelines for further development of self-regulation.

1. Legislation should not undermine self-regulation

As explained elsewhere in this report, the Board has rai-

sed two issues regulated by the Code which have been the subject of legislative initiatives with similar implications but less flexibility: Gender balance on boards of directors and decision making processes regarding senior management remunerations.

In both cases, there is a risk of confusing the conditions for political democracy with those of the market. It is vital that legislators do not limit or control the rights of owners to appoint people to represent them or restrict their abilities to compete for competence.

For those who seek to introduce certain systems or rules in all major companies, legislation has the advantage of covering a greater number of companies than is covered by the Code. However, as this report shows, the Code is applied by a much larger group in practice, having spread to a significant number of smaller listed and unlisted companies. Owners press for suitable solutions in each case. This shows that self-regulation works and leads to better corporate governance. Legislation is therefore unnecessary and parliament should be cautious about legislating on issues already regulated in the Code.

2. Nordic co-ordination of corporate governance codes

A further reason for legislators to refrain from detailed regulation is the process to harmonize the Nordic codes for corporate governance, initiated by the Board. Legislation and conditions of ownership in the Nordic countries are sufficiently similar that a single code may be possible in the future. Such a vision may be complicated and time-consuming to realize, but would make life easier for those companies that are listed in more than one Nordic country or would like to be so.

The international trend of greater demands on how large companies are run and how they behave will lead to numerous schools, principles and demands. Where such demands are an expression of individual actors’ considerations, they may reflect different investment philosophies and ownership principles, but when they are gathered into corporate governance codes for entire markets, or even national or European legislation, it is essential that there be as much co-ordination as possible.

3. Avoid unnecessary detail

It is clear from the debate surrounding the Code that there are some areas where the level of detail required by the Code is perhaps unnecessary. Any major review should avoid increasing the complexity and detailed regulation in the Code.

Lessons Learned in the First Year

Some of the concrete areas covered by the Code have already been the focus of discussion. After closer examination of these and a broader debate, the Board will decide whether to leave the issues raised until a larger review is carried out or whether more immediate solutions are required, as was the case with the issue of internal controls.

Two methods will be used in the short term to address the problems and opportunities that have been identified: Modification of the Code and/or development of appropriate practices within the existing framework of the Code together with those who work with the code in practice.

1. Modification of the Code

Modifications can take the form of changes in the text of the Code or of interpretations or instructions based on the existing text, and these will receive priority consideration by the Board. Any decisions will be announced in time for them to be applied during the following corporate governance season.

2. Development of good practice

By the development of appropriate practices we mean that the Board can initiate and encourage sharing of experiences where actors in the market can test and develop best practices.

The meeting held in December 2005 with a large group of owners, directors, company executives, experienced chairs of AGMs and selected advisers will be followed up by a similar meeting in 2006. The agenda will include areas where evaluation has shown that certain norms in the Code have been applied in different ways with different results. The aim is to spread knowledge about the smoothest solutions.

Issues for Continued Consideration in 2006

There are a number of problem areas that the Board intends to examine this year and consider whether action should be taken and, if so, whether they require modifica-

tion of the Code or the development of new practices. This section highlights three examples.

1. Improved annual general meetings

The increased use of proxy voting has led to a debate on how the ownership role should be exercised. Some reasons for this debate are that proxies for predominantly foreign institutional investors have sometimes voted against discharging boards from liability or against nominations to boards without providing reasons or offering alternatives; that decisions have been made by very small groups of attending shareholders following large numbers of abstentions; and that proxies have reported different voting records on the same issue to different owners. The questions raised by such behaviour should be addressed by the actors concerned, but they will also be discussed by the Board.

The Swedish Personal Data Act states that the wishes of any participants at an AGM not to have their names published in minutes that appear on the internet must be respected. This problem has often been solved relatively simply, whereas other cases have attracted a great deal of attention. This is a good example of how simple solutions should be spread to the wider community.

The Code does not address the hotly debated issue of whether it is appropriate for *the chair of a company to lead the annual general meeting*. The issue has generally been addressed by nomination committees in the companies covered by the Code. The result has been that the chair of the board has been elected as chair of the AGM in approximately half of the companies. The arguments for and against this solution take up the need for legal competence in certain situations, the importance of having a company chair who is visible and known to the owners and doubts about being able to combine the two roles when controversial issues are raised. Perhaps companies' experiences can be documented to help those who are considering the question for future meetings.

The Code offers the AGM the opportunity to *elect a nomination committee or determine a procedure* for how the nomination committee will be appointed for the next



meeting. In some cases, presentation of the procedure has been extremely detailed, whereas other companies have chosen provisional procedure to follow, thus reducing the need for oral presentations at future AGMs. Such flexible solutions can facilitate smoother, more efficient AGMs.

The report on the work of the board of directors and the presentation of complex proposals, e.g. incentive programmes, have in some cases consisted of *reading the written material aloud*, with a focus on procedures and legal details. At times, this has been perceived as quite time consuming. In other cases, the written material has been taken as read, and there has been a full presentation of the board's business discussions and a clear summary of the proposed rewards system. Perhaps the latter model can be developed into an accepted practice.

2. Areas where Swedish corporate governance may be difficult to understand fully in an international context

The appointment of *nomination committees* comprising owner representatives is unique in the international perspective. In the Anglo-Saxon model, a nomination committee is a committee within the board. Internationally, there is both scepticism and interest regarding the Swedish model, but it is uncertain whether other countries will develop similar solutions or whether owners outside Sweden may be prepared to participate in the work of Swedish nomination committees.

The issue of company directors' independence has been the focus of some debate. This partly concerns the definition of independence, where the Swedish code differs from most other codes, and partly the issue of how directors' dependence or independence is determined, as there appears to be some uncertainty regarding how the Code should be interpreted. The importance of this question will be heightened when the application of the Code is extended to smaller companies.

3. Rules that have proved difficult to interpret or apply

The *certification statement*, required in conjunction with the directors' signatures in the annual accounts according to the Code, has been widely discussed and has been

questioned by some as not adding anything to the legal liability requirements. At the same time, the Board notes that the vast majority of companies have found it reasonable to comply with this rule. Furthermore, it is likely that such a statement will be included in the legislation when the EU Commission's Transparency Directive is implemented in Sweden. The rule will then be removed from the Code.

The Board will evaluate the developments in reporting related to internal controls in Sweden and internationally. The Board will then consider whether there is a need for a separate report on internal controls or whether this can be included as a part of the Corporate Governance Report.

On the basis of this year's reporting season, the Board will also consider initiatives which aim to avoid overlap in corporate governance reporting and other parts of the annual report.

At the same time as conducting a deeper analysis of these and other issues, the Board will also be actively following the ongoing debate among those who work with and are affected by the Code.

Appropriacy and Usability

In conclusion, the Swedish Corporate Governance Board is convinced of the need for a Swedish corporate governance code. We will continue to promote this self-regulation model for improved corporate governance as a norm for more and more companies and to work to ensure that it is not undermined by detailed legislation.

The Board pays close attention to the appropriacy of different rules and will take initiatives regarding modifications or development of new practices if this can improve and simplify application of the Code. Any future review of the Code will be characterized by an ambition to avoid unnecessary complications for the work of multinational companies or owners and to meet strict demands for usability. ◀

The work of the Board 2005-2006

This chapter gives a general overview of the work of the Board during 2005-2006. More details about individual activities can be found on the Board's website, www.bolagsstyrningskollegiet.se.

The Role of the Board in Swedish Self-Regulation

The work of the Board is just one part of the corporate sector's self-regulation in the securities market. This regulation adopted a new structure in 2005, when the associations for stock market issues and for the development of generally accepted accounting principles, along with their underlying organs, were amalgamated to form the new Association for Generally Accepted Principles in the Securities Market. (See figure below.) The new Association is financed by fees from listed companies and its owners.

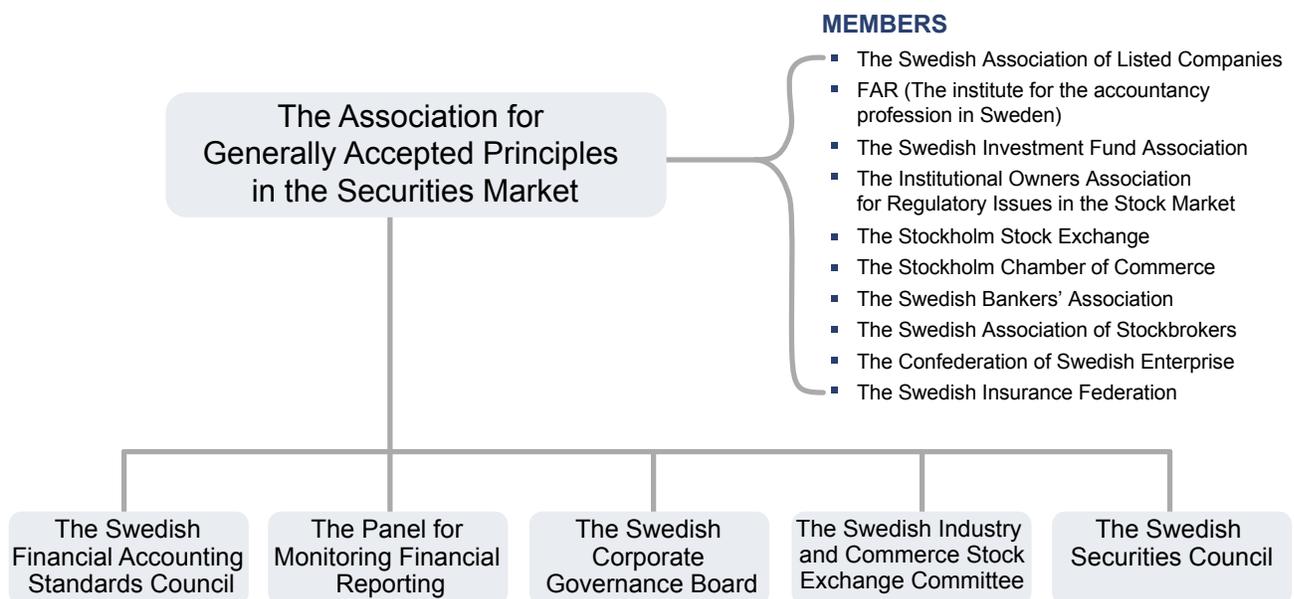
The aims of this change are to provide a better overview and to improve the efficiency of corporate self-regulation, as well as to ensure long term financing. There is

a strong tradition of self-regulation in corporate Sweden, designed to complement legislation with "soft regulation", which can often involve higher demands than those exerted by coercive rules. Swedish business and industry thus hopes to avoid unnecessary, far-reaching and unfocused legislation that may distort markets and restrict the growth and dynamics of business.

The Mission of the Board

The mission of the Swedish Corporate Governance Board is to promote the positive development of corporate governance in Sweden. Its role is to ensure that Sweden continuously has a relevant, modern, effective and efficient corporate governance code for listed companies, and it initiates and participates in discussion and debate on current corporate governance issues. The Board is also prepared to take part in international development work within the field.

The Board is responsible for determining norms for good corporate governance of listed companies. It does





this by monitoring and analysing how companies apply the Swedish Code of Corporate Governance on a general level and by making any changes to the Code that are then deemed necessary. The Board has no supervisory or adjudicative role regarding individual companies' application of the Code however. These roles belong to the Stockholm Stock Exchange and the actors on the capital markets respectively.

When considering the necessity for adjustments to the Code, the Board continuously monitors how it is applied through direct contacts with those responsible for corporate governance, such as owners, company directors, company executives, auditors, lawyers and other advisers. The Board systematically gathers and analyses the experiences of companies in their practical application of the Code. The Board also closely follows the general debate on the subject, changes in legislation and regulations concerning corporate governance, developments in other countries and academic research in the field. The Board always provides open information on its work and opinions.

The Work of the Board

Since its formation in February 2005, the Board has held eight minuted meetings. Much of the first half of 2005 was spent establishing the Board and its operations. A secretariat was set up, statutes and rules of procedure were formulated and a first version of the Board's website was developed. Subsequently, an increasing proportion of the Board's work has been devoted to actual matters of corporate governance. A general presentation of this work can be found in the next section. The goal of the Board's work is to create and maintain a high level of confidence in Swedish listed companies among Swedish and international investors and among the Swedish general public. To facilitate follow-up of this goal, a "Code Barometer" has been developed. This is a system to measure the attitudes of these target groups regarding Swedish corporate governance and the impact of the Code. To provide a basis for evaluation of future survey results, an initial base measurement was carried out in autumn 2005, and the results

were published on the Board's website. The aim is to conduct follow-up surveys at regular intervals.

In December 2005, the Board arranged a special meeting for representatives of companies and organizations affected by the Code. The aim was for the Board to have a direct dialogue with a number of people actively involved in corporate governance to hear their views on the Code and the future role and work of the Board. Around fifty people attended the meeting, and the discussion focused on three main issues:

- Confidence in the Swedish corporate governance model among foreign investors.
- How the Swedish Code of Corporate Governance is viewed by those who have started applying it.
- The Board's follow-up work on how companies apply the Code and which issues require special attention prior to any future review.

The main points covered and the Board's conclusions can be found on the Board's website. One of the topics of lively discussion was the Code's reporting requirements concerning internal controls. A number of companies had not had sufficient time to develop systems and routines to be able to report confidently on how well their internal control mechanisms had worked. It was also found that there is no clear and generally accepted framework that can be used for auditing these reports. As a result of this discussion, the Board issued a statement on the application of this rule in reports for 2005. (See next section.)

Throughout the year, the Secretary and members of the Board have participated as speakers and debaters at seminars and in other forums where Swedish corporate governance has been discussed. In June 2005, media representatives were invited to a seminar to raise awareness about the Code and Swedish corporate governance in general. More information on this seminar can be found on the Board's website. The Board has also been invited to present the Code and its application to a number of companies and organizations.

Key Issues Addressed During the Year

The Board has focused on a number of concrete issues in its first year. Here we present some of the most important.

The International view of Swedish corporate governance

In spring 2005, American corporate advisers ISS, (Institutional Shareholder Services), and the British index provider FTSE published a study which ranked a large number of companies in 24 countries in an FTSE ISS Corporate Governance Index based on companies' reporting for 2003. The majority of the 47 Swedish companies in the study received very low scores, and Sweden finished bottom of the list of countries analysed. The study was presented as a first step in the establishment of a system for rating companies according to the alleged quality of their corporate governance.

The Board contacted ISS and gained access to the material on which the study of the Swedish companies was based. Our analysis showed that the study has a predominantly Anglo-Saxon view of corporate governance and in many cases is based on misinterpretation or lack of knowledge of Swedish legislation and Swedish corporate governance. At the same time, there are a number of criteria on which Swedish companies could improve their ratings significantly through simple measures such as increased or improved reporting. As a service to the companies concerned, the Board distributed information on the FTSE ISS study and the Board's analysis, along with suggestions of how companies can avoid the most flagrant misunderstandings and undeserved negative assessments by relatively simple means. This material is available on the Board's website.

In April 2006, the Board gained access to a similar study based on companies' reports for 2004. This showed that Sweden was still well down the list of rankings, in 22nd position of 34 countries, and that the reasons for Swedish companies' poor ratings were essentially the same as in the previous year. The Board has now taken up a dialogue with ISS in order to explain more about corporate governance in Sweden and, as far as possible, to remove misunder-

standings and inaccuracies for future ranking of Swedish companies.

Gender representation at board level

In June 2005, the government set up an inquiry to present a proposal for legislation on gender representation on company boards of directors. The Board has voiced its strong objections to any such legislation, both to the inquiry and to the Ministry of Justice. These objections are outlined briefly in the previous chapter.

Internal controls

The rule that received most criticism during autumn 2005 was the Code's requirements regarding reports on internal controls. This was also the subject of much discussion at the aforementioned meeting in December 2005. Many companies had not had sufficient time to develop the necessary routines to be able to report reliably on how their internal control mechanisms had worked, and auditors expressed difficulty in analysing these reports due to the lack of a clear framework in which to work.

The Board acted upon these views and issued a statement on 15 December 2005 which allowed companies to limit their 2005 reporting to a description of how their internal controls were organized. They would not be obliged to report on how well the control mechanisms had worked nor to have the report audited. This initiative was positively received by the market, and a number of companies made use of this possibility.

Nordic harmonization of codes

During this first year, the Board, along with OMX, the owner of six Nordic stock exchanges, has initiated a dialogue with corporate governance representatives in other Nordic countries to discuss the possibilities of increased harmonization of the countries' corporate governance codes. The Board feels that such a development is extremely desirable, not only to make life easier for companies operating across Nordic borders, but also to support the ongoing integration of the Nordic stock exchanges. Common Nordic positions and activities would then have a



much greater impact on the development of the EU. One difficulty in the current circumstances is the differences in how the codes are administrated and organized in the four countries. Furthermore, not all countries have a formal code monitoring body with which discussions can take place. As a first step, the Board hopes that all Nordic countries will establish such bodies to act in further negotiations on these issues.

Legislation on remuneration of executive management

In autumn 2005, the Swedish government began work on a proposal for legislation to require AGMs to decide upon principles for top executives' remunerations packages and that these packages be presented on an individual level. The Board voiced objections to this, particularly the requirement of individual presentations of remunerations made to those below chief executive level. When the Bill was presented in April 2006, this requirement had been replaced by a requirement to provide a presentation of this level's collective remunerations, whereas the rest of the proposals remained largely unchanged. Since the Bill was presented, the Board has met the Parliamentary Standing Committee on Civil Law Legislation to express its continued criticism of resorting to legislation before the results of self-regulation in this field have been evaluated even provisionally.

Follow-up of the Application of the Code

As outlined above, one of the main roles of the board is to follow up and analyse on a general level how companies apply the Code in order to be able to consider future changes. As a first step, the Board conducted a survey in spring 2005 of the extent to which companies were already applying the Code at annual general meetings. This was of course before the Code even came into force. The results are presented on the Board's website. This survey was followed up this year by a similar survey of AGMs in 2006. The results and an analysis of the changes compared with 2005 are reported elsewhere in this report.

A central issue in the Board's follow-up is how companies apply the "comply or explain" principle and how this works in the Swedish media environment. The Board has therefore examined the corporate governance reports of all companies that are obliged to apply the Code and mapped all reported deviations and the explanations for them. The purpose of this is not to evaluate how individual companies have applied the Code, and the results will not be reported at that level. The key issue for the Board is to build up a picture of the extent to which different rules are being followed by the all companies using the Code or by different subsets, and to see what explanations are given for non-compliance.

In addition to these factual follow-up investigations, members of the Board have attended the AGMs of around thirty companies that are obliged to apply the Code. This has provided material for more qualitative assessments of how the Code has been applied at AGMs and how this has impacted the content and form of the meetings. ◀

APPLICATION OF THE CODE

To evaluate the application of the Code, the Board has initiated four studies to illustrate how the Code was applied by companies from its introduction on 1 July 2005 until the AGMs in 2006.

1. The Stockholm Stock Exchange has been invited to present a general outline of its view of how the Code has been integrated into the exchange's regulations and how it has been applied by companies so far.
2. The Board has commissioned Nordic Investor Services to conduct two surveys:
 - a) A compilation and analysis of companies' reporting of their application of the Code in the corporate governance reports they are obliged to include with the annual report, including a presentation of reported deviations and their explanations.
 - b) A survey of how certain aspects of the Code were applied at AGMs in spring 2006. How this has been done and any deviations that may have occurred are not always included in corporate governance reports, as these formally only cover the period up to the end of the calendar year. The study is a follow-up of a similar survey of AGMs in 2005, when the Code was yet to come into force, and it shows how application of the Code at AGMs has changed since then.
3. The Board has commissioned Anders Malmeby, a member of the Board, to make a summary of companies' reporting on internal controls regarding financial reporting. The rules of the Code on this issue were the subject of intense debate during autumn 2005, which led to the Board's statement on 15 December 2005 allowing companies to omit reports on how their internal controls had worked and freeing them from the obligation to have the report examined by auditors.



The Stockholm Stock Exchange – the First Year of the Code

Background

It was clear from the earliest stages of the development of a Swedish corporate governance code that both the authorities and the market had high expectations that the Stockholm Stock Exchange would take major responsibility for the implementation and application of the code. In its official comments on the Code Group's proposals, the Swedish Stock Exchange backed the introduction of a code and that the code should be an integral part of the Exchange's regulations. At that time, it was not possible to comment on this in greater detail, mainly because the Exchange wanted to consult with the Association of Exchange Listed Companies before giving a final opinion.

One of the issues that required discussion was whether the Code should be applicable to all listed companies or just for some. The result of this discussion was that the Code would initially apply to all companies on the Swedish Stock Exchange A-List and to the largest companies on the O-List, (those with a market value in excess of SEK 3 billion). This meant a total of around eighty companies. Foreign companies should apply the corporate governance code of their home countries or, where such a code does not exist, the Swedish Code. Information on the companies that apply the Code, voluntarily or in accordance with the regulations, can be found on the Stockholm Stock Exchange website www.se.omxgroup.com.

For those companies already listed, it was decided that the Code should be applied as soon as possible after 1 July 2005 and no later than at the first AGM after 1 January 2006. The thinking behind this was that companies would not need to have everything in place on 1 July 2005, something that would not have been feasible. Instead, the Code would be introduced successively and be applied in full by the 2006 AGMs. The Stock Exchange required the companies involved to include a corporate governance report as an appendix to the 2005 annual report. The term "apply the Code" means that the company shows actively how it fulfils the rules set out in the Code and reports this on its website according to the "comply or explain" principle.

With immediate effect from 1 July 2005, changes

were made to the Listing Agreement, the agreement made between listed companies and the Stockholm Stock Exchange. One of the changes stipulated that every company must have a section devoted to corporate governance on its website, not just those companies covered by the Code. This corporate governance information must be updated within a week of any changes that the company is aware of. The information must include whether the company applies a corporate governance code and if so which; up to date information on the composition of the board, including information on the individual directors; information on the Chief Executive; information on the auditors elected by the AGM; and the articles of association. Furthermore, a report on the work of the board during the previous year should be available on the website no later than the announcement of the AGM.

Inspection by the Stockholm Stock Exchange

The Stock Exchange's inspection of companies focuses on the obligations in the Listing Agreement and, to a certain extent, how companies comply with the listing requirements regarding application of the Code. The Exchange does not, however, evaluate the explanations given by companies for non-compliance with specific rules in the Code. This is left to the market. However, if it emerges that a company has provided incorrect or misleading information, this may cause the Stock Exchange to inspect the company more closely.

Application of the Code in Practice

Corporate governance information on the website

The surveillance department of the Stockholm Stock Exchange examined the websites of all the 251 companies on the Exchange between 15 and 25 November 2005. This revealed that 153 of the Swedish companies, or 60%, had a section devoted to corporate governance on their website. Of these, 102 companies stated clearly whether they intended to apply the Code or not. Many companies had not yet made a decision on the issue.

Of the 76 companies that were obliged to apply the Code, 25 had provided no information on the matter. Eleven companies had a section of their website devoted to corporate governance without actually remembering to state whether they were applying any code. Those companies without pages devoted to corporate governance were contacted by the Stock Exchange about this.

During spring 2006, a more detailed inspection took place to check whether discrepancies had been dealt with. Although many companies still had no section devoted to corporate governance, 239 companies, or 95%, did have information about the composition of the board on their website. Twelve companies had no information regarding articles of association on their website and fourteen companies had no or incorrect information about the Chief Executive of the company. The Stock Exchange contacted the companies concerned to demand that they make the necessary changes.

Of the twenty foreign companies listed on the Exchange, thirteen had a separate section of the website devoted to corporate governance. Nine of these companies stated that they applied a specific code, while four companies did not refer to a specific code but still provided information relevant to corporate governance. Three foreign companies stated that they apply a code voluntarily, and one of these applies the Swedish Code.

The Stock Exchange's preliminary examination of companies' annual reports shows that all companies that apply the Code have attached a corporate governance report and a report on the company's internal controls to the annual report. The reports are of varying quality, but this is to be expected and can largely be attributed to a lack of experience and the kind of teething troubles associated with the introduction of new rules and regulations.

Voluntary application of the Code

There has been some confusion among some groups regarding the extent to which the Code was applicable to the business year 2005. Despite this, the Code has received a positive reception from a number of companies. The 2005 annual reports of some companies not covered by the Code contain statements that the company has chosen to apply some or all of the Code. This is a positive development, but it should be borne in mind that a company which formally decides to apply the Code voluntarily will have a special status. The company must therefore notify the Exchange in writing about its decision. The company will then be added to the Exchange's list of companies applying the code. The commitment cannot be limited to a certain period of time, nor can it refer to only certain parts of the Code. So far, two companies, one Swedish and one foreign, have chosen such voluntary application of the Code. ◀

Anders Ackebo

Senior Vice President, Head of Surveillance
OMX Group



A Survey of Corporate Governance Reports and Annual General Meetings

– by Nordic Investor Services AB

Introduction

The Swedish Code of Corporate Governance has had a major impact on how companies report and how annual general meetings are conducted. Based on this survey, the following general conclusions can be drawn.

- The guidelines in the Code have already been widely accepted, both the rules concerning the annual general meeting and the rules in other parts of the Code.
- Some of the rules in the Code, which are actually more in the nature of suggestions, are unclear and have been misinterpreted.
- A total of 167 clearly reported deviations have been noted. Based on the 56 companies that reported at least one deviation, that gives an average of 3.0 deviations per company. If the 18 companies that reported no deviations are included, the average figure is 2.3 per company.
- Almost a quarter of all companies report no deviations at all, and around 19% report just one.
- Explanations of non-compliance are sometimes insufficient or non-existent.
- Annual general meetings in 2006 have been conducted almost completely with the guidelines in the Code, which is a significant change compared with the previous year.
- The content of corporate governance reports could be improved to make them clearer or more interesting. There has, however, been a great improvement in the information provided by companies regarding corporate governance issues.

The first part of this survey is based on the companies' corporate governance reports for 2005 and the deviations reported in these. The real extent of non-compliance is impossible to estimate, as it is not known how many deviations from the rules of the Code have not been reported. In the analysis, deviations that have not been specifically reported as non-compliance but have been inferred from the corporate governance report have been dealt with separately.

In the spring of 2005, Nordic Investor Services was commissioned by the Swedish Corporate Governance Board to conduct an analysis of how companies applied the rules of the Code at that year's AGMs, i.e. before the Code had become compulsory for the companies involved. Part 2 of this survey contains a follow-up of last year's study, which examined the same issues at the 2006 AGMs. This report is therefore divided into two sections:

- Part 1 examines corporate governance reports for 2005, including reported deviations from the Code and explanations for non-compliance.
- Part 2 examines the 2006 AGMs compared with those held the previous year.

Part 1 – Analysis of Corporate Governance Reports for 2005

Aims

Nordic Investor Services AB was commissioned by the Swedish Corporate Governance Board, (the Board), to conduct this survey in order to provide a general picture of how the Swedish Code of Corporate Governance was applied during 2005. The main focus has been on deviations that have been reported and the explanations given for non-compliance. An analysis of what other information has been provided in the corporate governance reports has also been made. The survey does not aim to analyse how individual companies have applied the Code, to rank companies according to how they have applied the Code or to find fault by scrutinizing whole annual reports.

Methodology and Companies Surveyed

A total of 78 companies fulfilled the criteria for compliance with the rules of the Swedish Code of Corporate Governance on 1 January 2006. For these “Code companies”, the Code is also part of their Listing Agreement with the Stockholm Stock Exchange. Since 1 January 2006, there have been a number of changes at Code companies, and this survey has corrected the information regarding TV4, which left the Swedish Stock Exchange during spring 2006. Of the 77 companies that provide the material for this survey, three have a split financial year, which means that their annual reports were not available during the survey period. These companies are not included in the survey, which is therefore based on 74 companies’ corporate governance reports.

The Code is not a set of obligatory regulations. It aims to provide guidelines for what is generally, though not necessarily always, regarded as good corporate governance in stock exchange listed companies. This flexibility in application is achieved through the principle of comply or explain, which is explained by rule 5.1.2 of the Code, which states *“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. 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.”

On this basis, the survey is based on the corporate governance reports in the annual reports for 2005 that were published before the end of May 2006.

Corporate Governance Reports

Corporate governance reports are a new feature in the annual reporting routines of Swedish companies. They are compulsory for all companies that are obliged to apply the Swedish Code of Corporate Governance and were first required in the annual reports for 2005. All 74 companies examined in this survey published a corporate governance report. Of the companies surveyed, only one has not explicitly stated that it applies the Code.

The corporate governance reports are of differing structure, quality and style. As the Code is applicable from 1 July 2005, some companies do not report deviations that have occurred before that time, while other companies have chosen also to report incidences of non-compliance in the first half of the year. This means that it is not possible to compare different companies exactly in this year’s survey. Comparison of future corporate governance reports will not be affected by this distortion.

Rule 5.1.1 of the Code states “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”

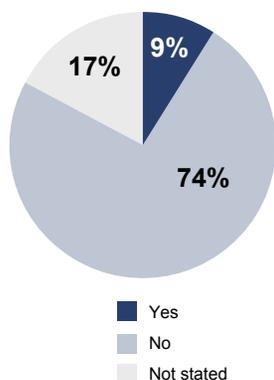
It is important to note that the latter is not a requirement, but it should be stated whether the report has been reviewed by the auditor or not. Of the 74 corporate governance reports in the study, 7, (9%), have been reviewed by the company auditor, 54 companies clearly state that the report has not been subject to auditor review and 13 reports do not indicate whether this has been the case or not, (see diagram 1).

Information in corporate governance reports

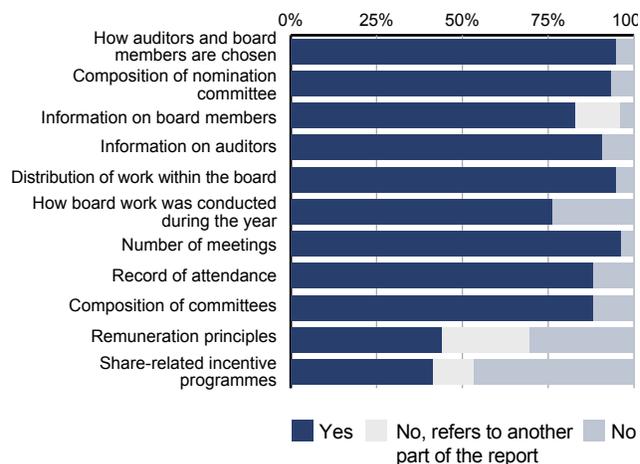
Rule 5.4.1 of the Code specifies what information should be included in the corporate governance report if it is not



Has the Corporate Governance Report been reviewed by the auditors? (diagram 1)



Corporate Governance Report contents (diagram 2)



provided elsewhere in the annual report. This is primarily information about the Board, its composition and its work during the year, but also information about the auditors, the Chief Executive and principles for the remuneration of the executive management, as well as other executive employment conditions. Many companies have chosen to be over-explicit and provide this information in several places in the annual report.

It may be of interest to examine to what extent companies have chosen to gather this information in the corporate governance report. Diagram 2 shows that corporate governance reports have generally been very informative in this respect. The only clear weakness is that 42% of the reports have not included information on remuneration principles or referred to other sections of the annual report. However, this does not mean that the information cannot be found elsewhere in the company's annual report.

Compared with previous years' annual reports, it is primarily information about the board and its work that has been developed as a result of corporate governance reports. It is interesting to note that information about board committees, attendance, number of meetings and composition of nomination committees is almost 100% complete. Furthermore, information regarding the

structure and organization of elections of directors and auditors has been improved. Information on the work of boards is often still scant however, and in some reports it is not reported at all.

It is a positive development that this kind of information is increasingly being made available to shareholders, contributing to greater transparency and understanding, even though the quality of reporting could be improved further and the information be more substantial.

Reported Deviations and Explanations

What constitutes a deviation?

The basis of this study is a survey of deviations from the Code reported by companies in their corporate governance reports. If a company has stated that it has acted in a way that does not conform to one of the rules in the Code, a deviation has been registered.

In most cases, this has been easy to identify, as companies have explicitly stated their non-compliance in the report. In some cases, non-compliance has not been clearly stated but has been apparent by reading between the lines. In cases where non-compliance has been deemed to be stated clearly enough, these have been included

in the total number of deviations but counted separately in the analysis of the number of deviations per rule.

For some rules, it has been difficult to determine whether a company's actions have constituted non-compliance or not. These rules are outlined briefly below.

Rule 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."*

An interim solution was presented for this rule in the Board's statement on 15 December 2005. This stated that it was sufficient for companies to limit their report on internal controls for 2005 to a description of how their internal controls were organized. They would not be obliged to report on how well the control mechanisms had functioned or to have the 2005 report reviewed by an auditor. A total of 62 companies (or 84%) referred to this interim solution.

All the companies investigated have included a report on how internal controls are organized and have therefore met the obligation set by the Board's statement. Separate reports were written by 45 of the companies, (see table 1). Elsewhere, the information has been included to varying degrees in the corporate governance report. One company had its report reviewed by the company auditor.

Although every company followed the interim rule that was applicable in 2005, 23 companies have reported this as non-compliance. On the basis of the Board's statement, this

has been seen as a misinterpretation of the rule and has therefore not been regarded as a deviation.

Rule 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."*

A total of 16 companies have reported non-compliance with this rule on the grounds that the expense was not justifiable and/or that the composition of company ownership did not require them to facilitate remote participation. As the rule carries these exceptions, the companies can be considered as following the rule without deviation.

Rule 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."*

Seven companies have reported non-compliance with this rule for various reasons related to the exceptions included in the text. As with rule 1.2.1, these deviations have not been regarded as non-compliance in this analysis.

Deviations per company

Of the 74 companies examined here, two state explicitly that they do not deviate from any rules. Another 16 companies have not reported any non-compliance or only reported non-compliance with the rule on internal controls. The latter group can be considered as not reporting any deviation, as they have met the requirements stated in the Board's interim solution for 2005. Assuming that all companies have followed rule 5.1.2 and reported all cases of non-compliance in the corporate governance report, this

Table 1

Is there a separate report on internal controls?	Number
Yes	45
Reviewed by auditors	1
Not reviewed by auditors	42
Not stated whether report has been reviewed by auditors	2
No	29

¹ A more detailed analysis of companies' reports on internal controls appears elsewhere in this annual report.



means that 18 companies, or 24%, followed all the rules of the Code in 2005.

Table 2 shows how companies have chosen to report non-compliance. It shows that the most common way is to include it in a separate section or as part of the introduction to the corporate governance report. A total of 39 companies (53%) have chosen one of these clear methods to report non-compliance. A further 11 companies report non-compliance clearly, but do so throughout the report where this is relevant. In 6 cases, it was only possible to identify non-compliance by reading between the lines in the text.

Table 2

Does the report state clearly which Code rules the company has not complied with?	Number	%
The company reports full compliance	2	3
No non-compliance reported	16	22
Yes, in a separate section	20	27
Yes, in the introduction	19	26
Yes, but not under one heading	11	15
No, only by implication	6	8

Companies grouped according to the number of stated deviations (diagram 3)

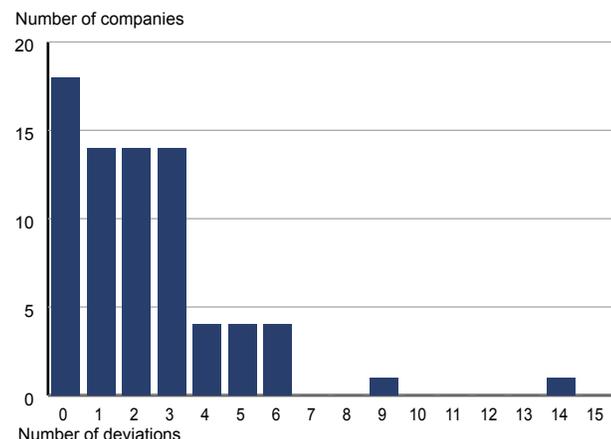


Diagram 3 shows the distribution of how many companies reported a certain number of deviations. It shows that 18 companies reported no deviations from the Code and 14 companies reported just one. One company reported nine cases of non-compliance and another had as many as 14. The diagram shows that the majority of companies reported 0-3 deviations from the Code.

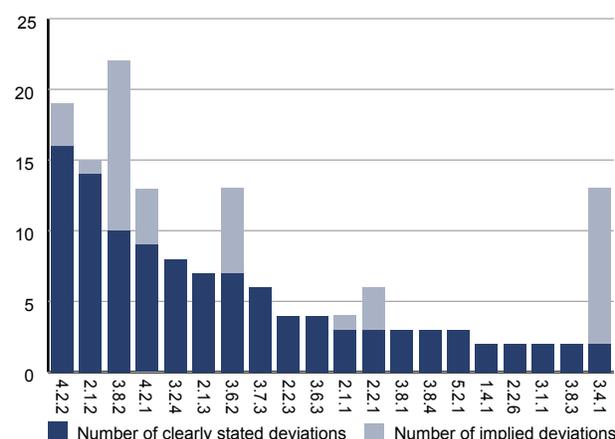
Deviations per rule

Diagram 4 shows the twenty Code rules where deviations have been noted most. The darker colour of each column represents clearly reported non-compliance and the lighter colour represents deviations that can be read between the lines.

As this analysis only covers non-compliance that is reported in the corporate governance reports, there is no assessment of whether there are further deviations which may be reported elsewhere in the annual report or not at all.

The analysis shows that 20% of companies have reported non-compliance with four particular rules. These are rules 4.2.2, 2.1.2, 3.8.2 and 4.2.1, which address reporting and decisions on remunerations principles at the AGM, the composition of nomination committees, auditing committees and remuneration committees.

Number of reported deviations (diagram 4)



Below, we analyse the explanations given for non-compliance with the ten rules for which companies have reported most deviations.

Rule 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 annual reports for 2005 primarily account for the 2005 AGMs. At that time, the Code had not yet come into force, which complicates the analysis. Of the 19 registered deviations, three were merely implied, while five companies have clearly stated that they will follow the rule as from the AGM in 2006. Part 2 of this report examines AGMs and how this and other rules were applied at this year's meetings. This shows that considerably more companies have raised this issue at the 2006 AGM compared with the previous year.

Of the remaining companies, eight have more or less the same explanation. These companies have referred to the Companies Act, which states that it is the responsibility of the board to make these decisions. The companies feel that transferring the right to make such decisions to the AGM could lead to confusion about responsibilities. Many of them have, however, informed their AGMs about their remunerations principles, even though this has not been a specific point for decision on the agenda.

Three companies have simply stated that they have not followed the rule, without providing any explanation.

Regel 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."*

One case of non-compliance with this rule can be classified as company-specific, and one company states that its clear ownership structure makes a nomination committee irrelevant and has therefore not appointed one.

The remaining 14 deviations are explained by certain board members being major shareholders in the company, making it natural for them to participate in the work of the nomination committee. In several companies, it is also regarded as natural that the chair of the nomination committee is also the largest shareholder, who is often also a member of the board.

Rule 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 ..."*

There has been some confusion surrounding this rule. As well as the 10 clearly reported and explained deviations, 12 deviations have been identified by implication. "

In each case, it has been reported that the whole board is also the auditing committee, with the occasional exception of the Chief Executive if he or she is also a member of the board. This complies with the second part of the rule, which states that small boards can act as auditing committees. There is, however, no clear definition of what constitutes a "small board", and this is an area open for interpretation. This means that it cannot be objectively established whether a company has deviated from this rule in the cases where the whole board functions as the auditing committee.

It is worth noting that a number of companies have not given any explanation of why the entire board also functions as the auditing committee. They simply state that this is the case.



Rule 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.”*

A number of the companies that report non-compliance with this rule state that their method of addressing remunerations issues is already satisfactory. Of these, seven companies say that their board places a premium on experience and continuity and therefore does not want to change the way in which remunerations issues are handled or the way the remuneration committee is formed. In one case, non-compliance with the independence criterion is reported with the explanation that the person concerned is a major shareholder in the company.

Rule 3.2.4: *“The majority of the directors elected by the shareholders’ meeting are to be independent of the company and its management ...”*

In two of the eight deviations reported, purely company-specific factors account for the non-compliance. In the other six cases, the AGM has decided that experience is more important than independence and therefore chosen not to comply with this rule.

Rule 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.”*

Seven companies have clearly reported non-compliance with this rule. In three of the cases, the time aspect is the common explanation. In certain cases, non-compliance is explained by the ambition to have an ownership structure that is as up-to-date as possible when deciding the composition of the nomination committee. In one case, the company explains that non-compliance is a result of the short period of time between its third quarter report and a relatively early AGM.

Rule 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.”*

Of the 74 companies included in this report, 61, or 82%, have a clear statement linked to the signatures in the annual report, (certification statement). Thirteen annual reports do not contain such a statement, and only seven companies have explained this non-compliance. One company states that the method for how this will be done will be formulated during the year and the rule will be followed from 2006. The other six companies state that this point is regulated by the Companies Act, and that a specific assurance statement in accordance with the Code would be unnecessary. A separate assurance is not needed, as the signatures of the board implicitly include such an assurance according to these companies.

Rule 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.”*

Of the six deviations noted, four companies explain the lack of an internal audit function by stating that the

existing organization and instructions are sufficient and that a specific control function is unnecessary. The remaining companies state that the issue is being investigated and that the rule will be complied with from 2006.

Rule 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 ..."*

This rule describes what information should be published regarding board members that are proposed for election or re-election and includes a number of items, from age and other assignments to share ownership and degree of independence.

Deviations from this rule have different explanations. In some cases, the nomination committee's proposals were not ready when the notice of AGM was sent out. One company states concentration of ownership as a reason for regarding both a nomination committee and broad information regarding proposed board members as unnecessary. Another company states that such detailed information has not previously been provided, but that it intends to apply this rule in the future.

Rule 3.6.3: *"The company's six- or nine-month report is to be reviewed by the auditors."*

All four companies that have reported non-compliance with this rule state that this rule will be applied from the current financial year.

Summary of Explanations of Reported Non-compliance

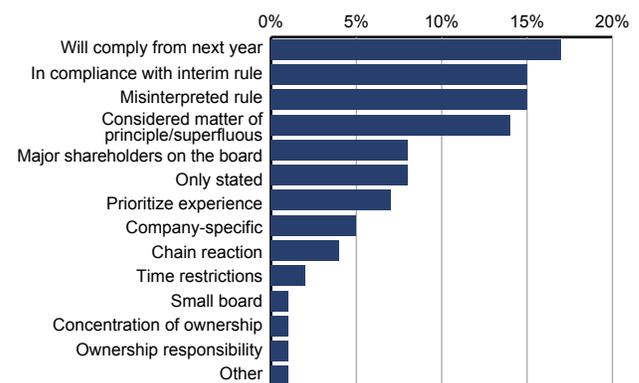
After reviewing all 74 corporate governance reports and the deviations reported, the explanations can be classified into 14 different categories. The results can be seen in diagram 5.

The diagram shows that the most common explanation is *Will comply from next year*, which is stated in around 17% of cases. Many of these cases concern auditor examination of six-month and nine-month reports, (3.6.3), and proposed principles for remunerations being approved by the AGM, (4.2.2). This explanation is also applied to areas such as the rules regarding nomination committees' proposals, (2.2.1), ethical guidelines, (3.1.1) and election of the Chair of the Board, (3.4.1).

There then follow two categories of explanations which have previously been defined as non-deviation: *In compliance with the interim rule*, which relates to the rule on reports on internal controls, (3.7.2); and *Misinterpreted rule*, which relates to the rules on remote participation, (1.2.1), and simultaneous interpretation, (1.4.3) at AGMs. Together, these categories account for 30% of all reported explanations.

These are followed by a number of categories that are more company-specific. One type of explanation, which is also relatively common, is that the rule in question is regarded as superfluous or that other principles are seen as more important to follow. These are shown under *Considered matter of principle/superfluous* and often refer to the board's responsibilities according to the Companies Act, the necessity of an "assurance statement", (3.6.2) or decision-making by the AGM on remunerations issues, (4.2.2).

Categorization of non-compliance (diagram 5)





The category *Major shareholders* on the board contains a number of cases where this is the main explanation of the composition of the nomination committee.

In the category *Only stated*, which accounts for around 8% of all reported explanations, non-compliance has been noted without any direct explanation. This relates most frequently to the board's establishment of an auditing committee, (3.8.2), but there are also deviations from the Code relating to AGMs deciding on principles for remunerations, (4.2.2), and to distribution of fees to board members, (2.2.6) which have not been clearly explained.

The category *Prioritize experience* is often an explanation for the composition of the board and deviation from the criterion of independence, concerning both composition of the board in general and of the remuneration committee.

Conclusions

Assessment of the 74 corporate governance reports has provided a detailed factual basis for an analysis of how the Code's guidelines have influenced companies and their reporting processes. This study has focused on the non-compliance reported by companies and the explanations given. Assuming good discipline in reporting non-compliance in corporate governance reports, it is clear that the Code has already achieved considerable acceptance among the companies that have applied it in its first year. Furthermore, a number of companies have stated that certain rules that were not complied with in 2005 will be followed from the current financial year.

The analysis has found over 200 deviations from the rules of the Code. Deviations resulting from misinterpretations have been excluded, as well as a number of reported deviations from the rule demanding a report on internal controls, as an interim solution changed this rule for 2005. That leaves 167 instances of actual non-compliance.

If these deviations are divided among the total number of companies reviewed, there is an average of 2.3

deviations per company. If the companies that have reported no non-compliance are excluded, (18 companies), the average is 3.0 deviations per company. Almost half of the companies, (43%), report no or just one deviation.

One general observation is that the non-compliance statistics are led by non-compliance with the rules governing committees, primarily the composition and/or mandate of auditing and remuneration committees, but deviations relating to the composition and mandate of nomination committees are also relatively common.

All non-compliance must be explained if a company is to be considered as applying the Code correctly, thereby conforming to the Listing Agreement of the Stockholm Stock Exchange. Despite this, the assessment has shown that there are a number of deviations from the Code that have not been explained. The explanations that have been provided are of varying quality. Some companies give clear explanations based on company-specific conditions whereas others are more brief or general. In some cases the explanation is simply that the rule in question is considered superfluous.

Part 2 – Application of the Code at Annual General Meetings in 2006

Aims

This part of the survey is a follow up to a corresponding survey conducted in spring 2005, which showed the extent to which certain rules in the Code had been applied by large companies listed on the Stockholm Stock Exchange at their AGMs in 2005. The aim of that survey was to provide a basis for future follow up of how implementation of the Code would affect the content and form of the meetings. A summary of the results can be found at the Swedish Corporate Governance Board website, www.corporategovernanceboard.se.

This survey of the 2006 AGMs is a follow up study to the survey of 2005. The 2006 survey is also a complement to the analysis of the 2005 corporate governance reports above. Formally, the 2005 annual report covers a company's application of the code in the second half of 2005, but not necessarily how it will be applied at the AGM in 2006. The companies surveyed have dealt with this issue in different ways. In some cases, companies have stated in the corporate governance report how they intend to apply the Code's rules at the 2006 AGM, whereas other companies have only reported this partially or not at all.

Methodology and Companies Surveyed

The main basis of this survey is company's notifications of 2006 AGMs. In some cases, this has been complemented by information from annual reports, websites, communiqués or direct contact with the company. The companies surveyed are all those that are obliged to apply the Code in accordance with the regulations of the Stockholm Stock Exchange, (Code companies), as well as all other companies on the Stockholm Stock Exchange Attract40 List.

The former group comprises the 78 companies that were obliged to apply the Code on 1 January 2006 according to the Stockholm Stock Exchange and that were still in this category at the time the survey was conducted. As with the survey of corporate governance reports in part 1 of this study, TV4 was excluded, since this company left the Stockholm Stock Exchange in the spring of 2005,

which leaves a total of 77 companies. The survey also includes companies with split financial years. The group "Other Attract40" comprises the 30 companies that were listed on the Stockholm Stock Exchange's Attract40 list but were not obliged to apply the Code.

The equivalent numbers for 2005 were 75 and 26 companies respectively.

The survey covers the following questions:

- Is there a nomination committee for this year's annual general meeting?
 - If yes, does the committee nominate the chair for the meeting?
 - If yes, who is nominated?
 - The Chair of the Board
 - Another person
- Does the annual general meeting elect the Chair of the Board?
- Does the meeting decide on remuneration of the Chair of the Board?
- Are the principles governing remuneration of the executive management presented at the meeting?
 - If yes, does the meeting decide on these principles?
- Does the meeting decide on a nomination committee for the next annual general meeting?
 - If yes, which method is used?
 - Establishment of a procedure for later appointment of members
 - Appointment of members at the annual general meeting

Survey Results – Code Companies

The results of the 2005 survey showed that many of the rules in the Code were already being applied by the majority of large companies on the Stockholm Stock Exchange. The main exception was the rule on presentation and decisions regarding the principles governing compensation and benefits to the executive management, which were only applied by a small number of companies.

Both the 2005 and 2006 surveys only report how companies have handled the above issues at the AGM. There has been no analysis of whether, and in which case how, non-compliance has been declared or explained. Below is a brief summary of the most important results of this year's survey compared with the 2005 results. A more detailed report is available on the Swedish Corporate Governance Board website.

Table 1 summarizes the results regarding the 2006 annual general meetings.

Nomination committee and election of the chair of the meeting

For 75 of the 77 Code companies, (97%), a nomination committee was in place before the 2006 AGM. This is an increase from 78% the previous year, (diagram 1a). The figures are similar for companies on the Stockholm Stock Exchange A List and the O List and for larger and smaller Code companies, (table 1).

In all but seven of these cases, (91%), the nomination committee has nominated the chair of the meeting, which is in accordance with the Code, (diagram b). The figure for 2005 was 63%. There is no great difference between companies of different size, although the figure is slightly higher for companies on the A List and for larger companies, (table 1).

In 50% of cases, the nomination committee nominated the Chair of the Board as chair of the meeting and in 50% of cases, the committee nominated another person, usually an external resource, (diagram 1c). The respective figures for 2005 were 55% and 45%, which means that there was a small increase in the proportion of external "professional" chairs. The proportions are exactly the same for companies on the A List and the O List. There is, however, a difference linked to company size, with 55% of larger companies choosing external chairs compared with 38% of smaller companies.

Table 1

Positive responses (%)	Code companies	Other Attract40	Code companies		Code companies	
	n=77	n=30	A List	O List	Larger ¹	Smaller ²
			n=45	n=32	n=51	n=26
Is there a nomination committee for this year's AGM?	75 (97 %)	26 (87 %)	44 (98 %)	31 (97 %)	49 (96 %)	26 (100 %)
If yes, does the committee nominate the chair for the meeting?	68 (91 %)	15 (58 %)	42 (95 %)	26 (84 %)	47 (96 %)	21 (81 %)
If yes, who is nominated?						
- The Chair of the Board	34 (50 %)	11 (73 %)	21 (50 %)	13 (50 %)	21 (45 %)	13 (62 %)
- Another person	34 (50 %)	4 (27 %)	21 (50 %)	13 (50 %)	26 (55 %)	8 (38 %)
Are the principles governing remuneration of the executive management presented at the meeting?	54 (70 %)	2 (7 %)	30 (67 %)	24 (75 %)	38 (75 %)	16 (62 %)
If yes, does the meeting decide on these principles?	52 (96 %)	1 (50 %)	29 (97 %)	23 (96 %)	37 (97 %)	15 (94 %)
Does the AGM elect the Chair of the Board?	76 (99 %)	24 (80 %)	45 (100 %)	31 (97 %)	50 (98 %)	26 (100 %)
Does the meeting decide on remuneration of the Chair of the Board?	77 (100 %)	24 (80 %)	45 (100 %)	32 (100 %)	51 (100 %)	26 (100 %)
Does the meeting decide on a nomination committee for the next AGM?	74 (96 %)	24 (80 %)	44 (98 %)	30 (94 %)	48 (94 %)	26 (100 %)
If yes, which method is used?						
- Establishment of a procedure for later appointment of members	63 (85 %)	23 (96 %)	37 (84 %)	26 (87 %)	40 (83 %)	23 (88 %)
- Appointment of members at the AGM	11 (15 %)	1 (4 %)	7 (16 %)	4 (13 %)	8 (17 %)	3 (12 %)

¹ Market value > SEK 10 billion

² Market value < SEK 10 billion

Election and remuneration of the Chair of the Board

The 2006 survey shows that all but one company chair was elected by the AGM, and in every case, the meeting decided on remuneration of the chair. The figures for 2005 were 58% and 77% respectively (diagrams 2 & 3). The only company that did not elect its chair at the AGM was a company on the O List with a market capitalization of more than SEK 10 billion.

Principles governing remuneration of the executive management

The biggest change from the previous year regards the Code rule on reporting and decisions on principles governing remuneration of the executive management. In 2005, 9 companies, (12%), delivered such a report to the AGM. This figure rose to 70% in 2006, (diagram 4a). Of the 54 companies that presented reports, 52 companies, (96%), decided on the principles governing remuneration at the meeting. The corresponding figure for 2005 was 67%, (diagram 4b).

There was no appreciable difference between companies on the O List and those on the A List, nor between larger and smaller companies, (table 1). In the two cases where AGMs did not decide on the principles, one was a larger company on the A List and one was a smaller company on the O List.”

Appointment of nomination committee

Decisions were made on the composition of the nomination committee for the 2007 AGM² in all but three companies, (96%). The corresponding figure for 2005 was 87%, (diagram 5a). All three companies that did not decide on this issue at the general meeting were large Code companies, one of which was on the A List and the others on the O List, (table 1).

Of the companies that did appoint nomination committees, a large majority, (85%), chose to follow procedures for later appointment of members, while 16% elected members at the AGM. The corresponding figures for 2005 were 85% and 15% respectively, (diagram 5b). Of the companies that elected members of the committee at the

meeting, there was a slightly higher proportion of A List companies and of larger companies, (table 1).

Survey Results – Other Attract40 Companies

As well as Code companies, the survey also includes companies on the Attract40 List that are not obliged to apply the Code. All of these companies had a market capitalization of less than SEK 3 billion in the previous 12 months. The results are summarized in the second column in table 1.

Although these companies are significantly smaller than most Code companies, they have chosen to apply the Code to a large extent. A total of 87% of these companies had a nomination committee in place for the 2006 AGM, and 58% of these committees nominated the chair of the meeting. There is, however, a significantly smaller proportion of external chairs than for Code companies, (27% compared with 50%).

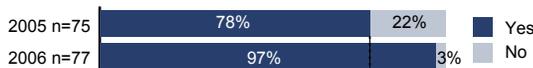
The majority of Attract40 companies have also chosen to apply the Code rules regarding election and remuneration of the Chair of the Board and the rules on nomination committees. A total of 24 companies, (80%), applied all of these rules. The method chosen differs sharply from that of Code companies however, with all but one adopting procedures for later appointment of members of the committee rather than electing members at the AGM.

The area in which Attract40 companies differ most from Code companies is that of reporting and deciding on principles of remunerations to the executive management at the AGM. Only two Attract40 companies have delivered such a report to the meeting, and only one of these meetings also decided on the matter.

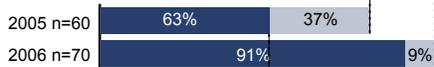
² In some cases, companies referred to decisions made at previous AGMs which were valid until further notice. In the survey, this has been classified as a decision on the composition of the nomination committee for next year's meeting.



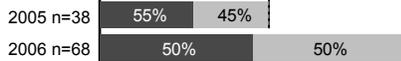
1a: Is there a nomination committee for this year's AGM?



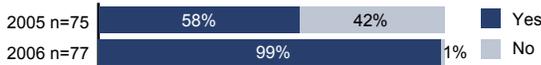
1b: If yes, does the committee nominate the chair for the meeting?



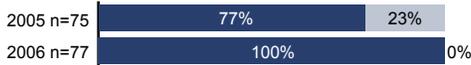
1c: If yes, who is nominated?
 - The Chair of the Board
 - Another person



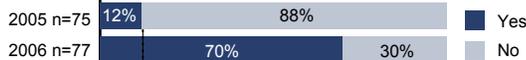
2: Does the AGM elect the Chair of the Board?



3: Does the meeting decide on remuneration of the Chair of the Board?



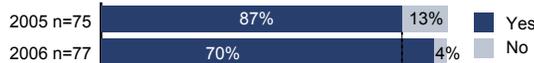
4a: Are the principles governing remuneration of the executive management presented at the meeting?



4b: If yes, does the meeting decide on these principles?

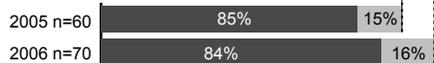


5a: Does the meeting decide on a nomination committee for the next AGM?



5b: If yes, which method is used?

- Establishment of a procedure for later appointment of members
 - Appointment of members at the AGM



Conclusions

A large number of Code companies had already applied many of the Code's most important rules regarding AGMs at their 2005 meetings. The main exception was the rules on presentation and decision on principles governing remuneration of the executive management, which were only applied by a small number of companies in 2005. At the 2006 AGMs, the rules on nomination committees, election of the chair of the meeting and the election and remuneration of the Chair of the Company were applied almost 100%, and application of the rules regarding presentation and decision on remunerations had increased to 70%. As a result, the Code can be regarded as having achieved a high degree of acceptance among companies.

Companies on the Attract40 List that are not obliged to apply the Code have also chosen to do so to a large extent. An important exception is the rules on presentation and decision on remunerations at the AGM, which were only applied by two Attract40 companies. This, along with the low proportion of voluntary application of these rules among Code companies in 2005, indicates significant resistance to this rule among many companies.

Helena Levander

Chief Executive Officer, Nordic Investor Services

Company Reports on Internal Controls, 2005

Background

Companies which are covered by the Swedish Code of Corporate Governance must, from the financial year 2005, submit an annual report on how internal controls regarding financial reporting are organized. The board must also report on how well the controls have functioned in the previous financial year. The report must be reviewed by the company's auditor.

If the company does not have an internal audit function, the Code states that the board must evaluate the need for such a function annually. The report on internal controls must then include an explanatory statement from the board on the outcome of this evaluation.

The Swedish Corporate Governance Board issued a statement on 15 December 2005 explaining that there may be circumstances that make full compliance with the Code's reporting obligations difficult in the 2005 report, e.g. the introduction of International Financial Reporting Standards, (IFRS), difficulties in formalizing company processes quickly and a lack of guidelines for auditing the reports. The Board announced that a description of how the internal controls are organized would suffice in the 2005 report, and a statement on how well the controls had functioned would not be required. Nor would the report need to be reviewed by the company's auditor.

Summary of Survey Results

How have companies handled reporting of internal controls in 2005? To find out, all companies that were covered by the Code as of 1 January 2006 and that had the calendar year as financial year have been surveyed. The conclusions can be summarized briefly as follows:

- The Code's rules on internal reporting have had a major impact. All surveyed companies have submitted a report.
- Most reports are structured in such a way that makes them easy to read. In most cases, the structure follows the recommendations of the Confederation of Swedish Enterprise and FAR (the institute for the accountancy profession in Sweden).

- Following the Board's statement of December 2005, over 80% of the companies have restricted their reporting to a description of how internal control mechanisms are organized, without evaluating how well they have functioned during the financial year
- A small number of companies have submitted an evaluation of their internal controls. One company has also filed an auditor's report on how the controls have functioned.
- Virtually all companies have fulfilled the Code's demand for an assessment of the need for an internal audit function.
- The highest levels of ambition in this area were shown by larger companies (on the Stockholm Stock Exchange A List), companies listed on a US stock exchange (SEC listed companies), and banks.
- There is great variation in the ambition levels of companies on the stock exchange O List. Ambitions are significantly lower than among companies on the A List.
- The number of reports with descriptions that are not sufficiently related to the company's own operations is greater among O List companies than among those on the A List.
- Companies with ambitious reporting levels have consistently submitted separate reports on internal controls. More than half of these state that they have used the COSO³ framework in their internal work to develop internal controls.
- In general, the reports on internal controls are about a page long. The most detailed is four pages long.

The Survey

The aim of the survey is to follow up companies' reports on internal controls for 2005. The survey includes 74 of the 78 companies on the Stockholm Stock Exchange A List and O List that were covered by the Code on 31 December 2005 according to the exchange. Of the 74 companies in the survey, 43 are on the A List and 31 are on the O List.

One of the companies was moved to another trading list not covered by the Code in spring 2006. This company

³ The Committee of Sponsoring Organizations of the Treadway Commission.



was therefore excluded from the survey. Three companies were not included because they had split financial years.

Results

Information included in a separate report or in the corporate governance report

Table 1 shows that all surveyed companies submitted a report on internal controls, either in a separate report or as part of the corporate governance report.

Report structure

The survey found that 56 companies chose to structure the information on internal controls in accordance with the guidelines issued by the Confederation of Swedish Enterprise and FAR 2005⁴. Of companies on the A List, 77% followed the guidelines, compared with 74% of companies on the O List.

Describing internal controls without evaluating

The Swedish Corporate Governance Board's statement

of 15 December 2005 allows companies to limit their reporting on internal controls to a description of how they are organized, without providing an evaluation of how well they have functioned during the financial year. Table 2 shows that a large number of companies took advantage of this opportunity. Other companies have limited their reporting in the same way but without reference to the Board's statement.

Companies that have submitted an evaluation

Five companies have submitted some form of evaluation related to the information on internal controls. Three of these companies are on the A List and two are on the O List.

The evaluations are expressed in different ways. One company states that its internal controls are "good", another that its controls are "appropriate" and a third uses a combination of the two. A fourth company expresses its assessment in terms of risk and a fifth uses the term "well balanced control structure".

Table 1: Method of reporting information on internal controls

	A List		O List		Total	
	Number	%	Number	%	Number	%
In a separate report on internal controls	28	65	17	55	45	61
In the corporate governance report	15	35	14	45	29	39
	43	100	31	100	74	100

Table 2: Reference to the Swedish Corporate Governance Board's statement of December 2005

	A List		O List		Total	
	Number	%	Number	%	Number	%
Companies that only describe internal controls, with reference to the Board's statement	37	86	25	81	62	84
As above, but without explanation	5	12	5	16	10	13
Companies that refer to the Board's statement, but also present a description and an assessment	1	2	1	3	2	3
	43	100	31	100	74	100

⁴ Board reports on internal controls regarding financial reporting, guidelines on the Swedish Code of Corporate Governance, issued by working groups at the Confederation of Swedish Enterprise and FAR, 17 October 2005.

Auditor review

In one case, a company which submitted an evaluation of its internal controls also submitted an auditor’s report.

Assessment of the need for an internal audit function

According to section 3.7.3 of the Code, boards of companies without an internal audit function must assess the need for such a function each year. The report on internal controls must include a statement explaining the board’s decision. Almost all companies, (95%), have submitted such an explanation. This also includes companies that have an internal audit function or the equivalent.

Two companies on the A List and three on the O list have not reported whether they have conducted an evaluation. One of these states that methods for this will be developed during the coming year. This should be regarded as an explanation, meaning that the Code rule has been followed. The remaining four companies have not provided an explanation.

Level of ambition

Companies’ levels of ambition when reporting on internal controls has been assessed in the survey, both where reports have been written separately and when they have been a part of the corporate governance report.

The reports have been divided into three categories: Low, Medium and High. The reports in the High category are characterized by detail, substance, transparency and clear reference to the company’s operations. Reports in the Low category are brief and contain information of a highly standardized nature.

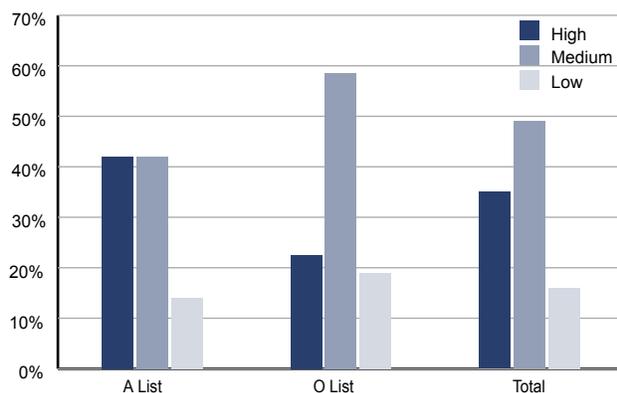
As can be seen in table 3, ambition levels were higher among A List companies than among those on the O List. Assessment of these criteria contains a degree of subjectivity however, and this should be considered when assessing the precision of the results.

Table 3 also shows a positive link between companies with high levels of reporting ambition and submission of separate reports on internal controls. ◀

Table 3: Reports of companies with high levels of reporting ambition:

	A List		O List		Total	
	Number	%	Number	%	Number	%
Companies with a separate report on internal controls	16	84	5	71	21	81
Companies which only publish the information in the corporate governance report	3	16	2	29	5	19
	19	100	7	100	26	100

Level of ambition in the reports



Anders Malmeby

Member of the Swedish Corporate Governance Board.