

Corporate Governance Code Proposed

1. Corporate Governance Code

Recent international and Swedish corporate scandals have affected the general public's confidence in Swedish business and led to a negative view of the corporate world. In order to rebuild impaired trust, in September 2002 the Swedish government established a commission on business confidence with a mandate to identify potential concerns and propose solutions. The following principal priorities were pinpointed by the commission:

- improved corporate governance;
- increased confidence in the financial markets;
- more effective competition policies; and
- focused efforts on white collar crime.

With particular emphasis on corporate governance, certain members of the commission, together with selected representatives of the Swedish business sector, were asked to draft a corporate governance code. This has resulted in the proposed Swedish Corporate Governance Code, while the other prioritized areas were dealt with in an official governmental report.

Scope and applicability

While certain countries have resorted to legislation, such as the United States through the Sarbanes-Oxley Act, Sweden intends to address corporate governance primarily through strengthened self-regulation. Thus the code is not intended to be binding but is based on self-regulation and the 'comply or explain' principle, which allows deviation where reasonably motivated. Influences for the code include its British equivalent, the Cadbury Code.

The Swedish code is primarily intended to be applied by Swedish limited liability companies listed on a Swedish exchange or authorized marketplace. However, according to the code, the rules it proposes are also relevant to other categories of companies with broad ownership and/or public interest. These include certain state or municipally owned companies and larger privately held corporations.

Entry into force

The code is expected to enter into effect in early 2005, after comments on the proposal which has been circulated for consideration have been evaluated and incorporated into the

code. Thus the proposed provisions may to some extent be altered when the final version of the code is adopted.

Principal features

The principal features of the code are as follows:

- It contains general rules with respect to corporate governance and provides a structural framework for these matters;
- It emphasizes the importance of strong ownership influence over the conduct of business through assigning various powers and control functions to shareholders;
- It proposes measures for the clarification of the allocation of liabilities and responsibilities between different corporate bodies; and
- It addresses certain financial reporting and audit matters.

These four cornerstones are expected to be achieved through the implementation of a number of measures.

Shareholders meetings

The code introduces stricter requirements with regard to the information to be provided in notices to shareholders meetings, as well as when such information must be made available. Furthermore, a mandatory participation requirement for the board of directors, the management and the auditor at shareholders meetings is prescribed. Together with certain additional measures, these requirements are expected to strengthen shareholder influence.

Size of the board of directors

A limitation is introduced, capping the maximum number of board members to nine. No deputies may be elected.

Composition of the board of directors

Diversity with regard to experience and personal background, and an even distribution between male and female board members, are proposed.

Proposals for the re-election of members who have been members of the board for eight years or have reached the age of 70 must be explicitly justified.

Independence of the board of directors

A majority of the board members must be independent from the company (eg, with regard to employment, shareholdings and business relations) and the management of the company, and at least two of these board members must also be independent of larger shareholders of the company.

Informed boards of directors

Introductory briefings to new board members are proposed.

Appointment of board members, chairman and auditors

The nominations committee shall present to the shareholders meeting proposals for the chairman, other board members and auditors.

The chairman of the board shall be appointed by the shareholders meeting (and not, as currently, by the board of directors). The chairman of the board may not act as the chairman at shareholders meetings, the chairman of the nominations committee or the audit committee, nor be employed full time as group chief executive officer.

Remuneration of the board of directors and management

It is proposed to establish a nominations committee to prepare for the election of board members and the chairman, and to prepare the principles of remuneration with regard to the board of directors, the chairman and the auditors. Based on the proposal prepared by the nominations committee, the shareholders meeting will decide on the remuneration to the board.

It is proposed to establish a remuneration committee to prepare for the remuneration of the managing director and other management. The remuneration principles will be adopted by the shareholders meeting. Based on these principles, the board of directors can determine the remuneration of the managing director.

All share or share price-related incentive programmes shall be resolved by the shareholders meeting.

Evaluation of the board of directors, chief executive officer and auditors

The work of the board of the directors and the chief executive officer will be subject to annual evaluation - the former by the nominations committee and the latter by the board of directors - without the participation of the chief executive officer. Furthermore, the auditor of the company will also be evaluated.

Financial reporting and auditing

The board shall certify in writing that the annual accounts, to the best of their knowledge, have been prepared in accordance with generally accepted accounting practices for stock market companies, that the information presented is consistent with actual conditions and that nothing of material importance has been omitted.

The chief finance officer shall certify in writing that the company's financial reporting - the annual as well as the quarterly reports - meets the requirements of applicable rules and regulations.

An audit committee will be established. The audit committee shall examine and report critical accounting issues and review all financial reports.

Internal audit functions will be established.

A specific report on the governance of the company shall be included in the annual report and posted on the company's website.

At least one interim report should be reviewed by the auditors.

Penalties and supervision

There are no formal penalties for violating the code, but non-compliance may result in considerable market ill will. The Stockholm Exchange is expected to include the code in its listing agreement and thus make the standards in the code binding upon companies listed on the Stockholm Exchange. It has been suggested that a non-profit association, a body tentatively named the Council for Swedish Corporate Governance, will administer the code.

Criticism

The code is currently being circulated for comments and it can be expected that some of its proposed features will be modified or altered. The code has been criticized for not using a coherent terminology compared to expressions employed in legislation, and for duplicating existing legal or regulatory requirements, in some instances with minor changes, thereby creating uncertainty as to the applicability of the current rules and regulations. Some of the proposed measures in the code (eg, the confirmation from the board of directors and the chief finance officer with respect to the accuracy of the company's accounts) have also generated debate as to whether the code intends to or will broaden directors' and management's liability.

2. Proposed Legislation

The commission has also proposed that some measures in the code lead to changes in the Swedish Companies Act and the Annual Accounts Act, as applicable, and thus become

mandatory legal requirements. Therefore, the passing of resolutions with respect to various forms of remuneration for management and the board of directors (including general principles governing remuneration, fees, and their allocation and incentive programmes) should be the exclusive prerogative of the shareholders meeting. Furthermore, it is proposed that legislation be introduced with respect to certain information requirements on the reporting of the remuneration of key employees and the board of directors. It has also been suggested that provisions regulating the election of the chairman of the shareholders meeting, the definition of the role of the nominations committee and a limitation on the presence of union representatives at board meetings be incorporated into the Swedish Companies Act. Finally, the assurance provided by the board of directors and the chief finance officer with regard to the financial reporting has been put forward to become the subject of legislation.

3. Strengthening Confidence

Apart from the code and the proposed legislation, certain additional confidence-building measures have been proposed in the official government report. These proposals include the following:

- The Swedish Accounting Standards Board and the Supervisory Board of Public Accountants will be closed down, with a new governmental supervisory authority, the *Redovisningsinspektionen*, responsible for accounting and auditing;
- The limitations on the ownership interests of Swedish national pension funds and the limitations on the rights of the seventh Swedish pension fund to vote for shares held will be reviewed in order to abolish these restrictions;
- A more distinct ownership role will be created within the state-owned company sector. The management of companies wholly or partially owned by the state should be concentrated within the Ministry of Industry, Employment and Communication;
- The wealth tax will be abolished;
- The Financial Supervisory Authority will be principally responsible for consumer protection within the financial arena;
- Administrative penalties in the form of fees will be introduced in the event of misleading marketing of financial services;
- Regulations on conflicting interests in companies dealing with securities corresponding to the US Spitzer Rules will be introduced;

- Self-regulation within fund companies and the securities market should be strengthened;
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- The government should investigate how business activities can be clearly separated from the legislative and surveillance functions of the Stockholm Exchange and other authorized marketplaces; and
- Various actions will be taken against white collar crime.

These proposed measures are not expected to enter into force in the near future.

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