Unofficial translation

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Consultation: The Norwegian Code of Practice for Corporate Governance

The Norwegian Corporate Governance Board (NCGB) invites all interested parties to provide any comments they may have on the Norwegian Code of Practice for Corporate Governance (the "Code"), and asks that comments be submitted by 1 September 2012.

NCGB issues revisions to the Code as required. The most recent printed edition of the Code was published in 2010, but some limited changes were subsequently made in the form of a document issued by NCGB on 20 October 2011, which is published on the NCGB website.

The attachment to this letter sets out the preliminary views of NCGB on the issues that it may be appropriate to incorporate into the Code. The most substantial of the proposals relate to:

- More detailed explanation of the 'comply or explain' principle.
- The justification for the nomination committee's recommendations.
- The content and public disclosure of transaction agreements entered into in connection with takeovers.

In its work on the continuing development of the Code, NCGB wishes to encourage as many interested parties as possible to put forward their views, comments and proposals, not only in response to the consultation attached to this letter but also in general. This feedback will be valuable for NCGB in its continuing work and for subsequent revisions to the Code. NCGB is of the opinion that there are no changes in legislation that currently require changes to the Code. No decision has yet been taken on whether to issue a revised version of the Code in printed form this year. If a new version is published, the changes made in 2011 mentioned above will also be included.

Please send your responses to info@nues.no. Responses to the consultation will be published on the NCGB website.

We would like to take this opportunity to remind recipients of this year's NCGB Corporate Governance Forum, which will take place on the morning of 23 October at Næringslivets Hus in Oslo. The Forum will include a presentation of any changes to the Code that are approved following the consultation exercise. The final program for the Forum will be published on the NCGB website nearer the time.

Yours faithfully

Ingebjørg Harto
NCGB Chairman

1. ‘Comply or explain’ principle (page 7 and Section 1)

The Accounting Act includes a statutory requirement for companies to provide a report on their policies and practice for corporate governance with effect from the 2011 financial year. NCGB amended Section 1 of the Code in the document issued on 20 October 2011 to incorporate this change.

The Code is in principle intended to address matters that are not already regulated by legislation, although for the sake of completeness the Code does include some exceptions to this principle. In other words, in almost all areas the Code seeks to address relevant matters *more comprehensively than is required by legislation.* This is also the case for the *content of the reporting*, where the Code stipulates requirements that are more comprehensive than required by legislation. It would appear that some companies do not fully appreciate this principle behind the Code. NCGB accordingly proposes making changes to clarify how companies should report, both when they comply with the Code and when they explain some other approach.

NCGB accordingly proposes the following change to the wording of the section *Adherence to the Code of Practice – "comply or explain"* (page 7) as follows:

> "Adherence to the Code of Practice will be based on the "comply or explain" principle, as explained in further detail in the commentary to Section 1 of the Code of Practice." ~~whereby companies must either explain how they comply with each of the recommendations that make up the Code of Practice or explain why they have chosen an alternative approach.~~"

NCGB is of the view that the requirements for the "comply or explain" principle will be more easily accessible if they are set out in the context of Section 1 of the Code. The following changes are therefore proposed to the wording of the commentary to Section 1:

> "The requirement for reporting corporate governance is based on the "comply or explain" principle ~~as explained in the introduction~~. The Accounting Act stipulates that issuers listed on a regulated market in Norway must provide a report on their policies and practice for corporate governance. In the event that a company deviates from the requirements of the Code of Practice, the Act stipulates that the company must provide a justification for such deviation. The requirements of the Code of Practice are more comprehensive than the statutory requirements: Firstly, the report must cover every section of the Code of Practice. This means that companies must provide information on the sections with which they comply as well as on the sections from which they deviate. Secondly, a company that does not comply with the Code of Practice must, in addition to providing the justification required by the Accounting Act, explain what alternative solution it has selected."

2. Use of board mandates for the issue of shares (Section 4, second paragraph)

Section 4, second paragraph of the Code stipulates that any decision to waive the pre-emption rights of existing shareholders in the event of an increase in share capital "must" be justified when the board issues shares. In addition, this justification "must" be publicly disclosed in a stock exchange announcement. In accordance with the convention used in the Code for the use of "should" and "must" (see page 8), NCGB proposes changes to the wording of this section so that the board's decision to waive pre-emption rights in the event of an increase in share capital "should" be justified, and the justification "should" be publicly disclosed in a stock exchange announcement. The effect of this will mean that issuers which choose not to provide a justification when the board decides to waive pre-emption rights when issuing shares will be required to explain why they have elected not to provide such a justification.

3. Justification for the nomination committee's recommendations (Section 7, fifth paragraph)

It has become apparent that some nomination committees do not provide a justification for their recommendations in the manner recommended in Section 7, fifth paragraph of the Code. The commentary to Section 7 (page 27) primarily mentions information on the candidates, and it would

appear that this may lead some nomination committees to neglect to address other elements in their justification, such as how the candidates proposed will satisfy the company's requirements in respect of expertise.

NCGB is of the opinion that the wording of Section 7 is already sufficiently clear, but that the commentary to this section should provide even greater clarity on the need for the nomination committee's justification of its recommendations to address matters such as the interests of shareholders in general and the company's requirements in respect of expertise, capacity and diversity, cf. Section 8 on the composition of the corporate assembly and board of directors. NCGB therefore proposes the following changes to the wording of the commentary:

> "In accordance with Section 6 above, the nomination committee's recommendations and report should be made available in accordance with the 21-day deadline for the notice calling a general meeting. The report should provide a justification of how the committee's recommendations take into account the interests of shareholders in general and the company's requirements in respect of expertise, capacity and diversity, ~~The committee's recommendation should include relevant information on the candidates,~~ cf. Section 8 on the composition of the corporate assembly and board of directors. ~~The recommendation~~ The justification should accordingly include information on each candidate's competence, capacity and independence. Information on the ~~members of the board of directors~~ candidates should include each individual's age, education and business experience. Information should be given on how long each individual has been a member of the board of directors and any assignments carried out for the company, as well as the individual's material appointments with other companies and organisations. ~~In the case of a proposal for re-election, the recommendation can refer to the information already provided in the annual report.~~
>
> The recommendation should also include relevant information on the candidates for election to the nomination committee."

4. Composition of the corporate assembly and board of directors (Section 8, first and second paragraphs)

The first paragraph of Section 8 of the Code addresses the composition of the corporate assembly for companies that have this type of corporate body. This paragraph should not be interpreted as a recommendation that companies should have a corporate assembly, and it is not the intention that companies that do not have a corporate assembly should be required to explain this as a deviation from the Code. However, it appears that some companies have adopted this incorrect interpretation of this paragraph. NCGB accordingly proposes to clarify this situation by including a new paragraph under the heading "Composition of corporate assembly" in the commentary to Section 8 as follows:

> "Companies that are not required have a corporate assembly pursuant to an agreement with their employees or a ruling by the Corporate Democracy Commission should provide information in this respect."

The Public Limited Companies Act includes a provision at Section 6-3 that permits the right to elect members of the board of directors be transferred to a body other than the general meeting. NCGB takes the view that the election of the members of the board of directors is a matter for decision by the company's owners at a general meeting (with certain exceptions in respect of companies with a corporate assembly and where some members of the board of directors are elected by employees). In order to clarify this, NCGB proposes that the following sentence should be added at the end of the section of the commentary headed "Composition of the Board of Directors" on page 29.

> "The Public Limited Companies Act permits the transfer of the right to elect members of the board of directors to a body other than the general meeting. The company should not exercise the option to transfer this right away from the general meeting."

5. Reporting on risk management and internal control (Section 10)

Section 10, third paragraph of the Code stipulates: "The board of directors should provide an account in the annual report of the main features of the company's internal control and risk management systems as they relate to the company's financial reporting". With effect from the 2011 financial year, Section 3-3b of the Accounting Act stipulates that companies must provide "a description of the main elements in the enterprise's, and for entities that prepare consolidated financial statements, if relevant also the group's, internal control and risk management systems linked to the financial reporting process". The wording in the Act accordingly differs somewhat from the wording in the Code.

The requirement stipulated in the Accounting Act applies to companies for which Norway is the home state. In practice, listed companies for which Norway is the host state will also be subject to equivalent requirements in their home state because this requirement is a consequence of the EU Accounting Directive. Since all companies listed in Norway are required by law to provide the description mentioned above, NCGB proposes deleting Section 10, third paragraph from the Code.

The section of the commentary that deals with this issue under the heading "Reporting by the Board of Directors" (page 41) will continue unchanged, but will be preceded by an explanation that the account to be provided in the annual report is a statutory requirement.

The first paragraph of Section 10 and the related commentary serve as a clarification of the Accounting Act's requirements in respect of the responsibility of the board of directors for ensuring sound risk management and internal control systems. NCGB proposes that this should be explained in the footnote.

6. Take-overs (Section 14)

Changes were made to this section in 2010 so that it now principally addresses the target company and its board of directors. However, take-overs encompass a wide range of situations, with considerable differences between the legal requirements that apply. For example, a mandatory offer is subject to relatively comprehensive legal regulation, but the handling of a voluntary offer is largely a matter for the bidder and for the board of directors of the target company, depending to some extent on whether the offer is recommended or is 'hostile'. This makes it difficult to produce recommendations that cover every situation while at the same time providing sufficiently clear and concrete guidance.

NCGB has the impression that it has become increasingly common in recent years for the board of the target company to enter into an agreement with the bidder when a voluntary offer is made for the company that the board recommends. Such agreements typically include provisions whereby the board will recommend the offer to shareholders, the bidder will be given access to information that is not in the public domain (due diligence) and agreement that the target company will pay financial compensation to the bidder if the bid does not proceed ("break fee"). A further area that may be subject to agreement is the company's response to any competing bids, including the question of whether the company can itself initiate such a competing bid ("no shop"). Such an agreement may also address a number of other issues, for example the future relationship between the bidder and the target company on the one hand, and on the other hand the future arrangements for the executive management of the target company.

Such agreements may be of great importance for shareholders and the market when evaluating the offer. The Code already provides commentary on this area, including (page 49):

> "The board must exercise caution in agreeing to any commitments by the company that may make it more difficult for competing bids to be made or that may hinder any such bids. Such commitments, including commitments in respect of exclusivity ("no-shop") and commitments in respect of financial compensation if the bid does not proceed ("break fee") should be clearly and evidently based on the shared interests of the company and its shareholders. Any agreement for financial compensation to be paid to the bidder should, in principle, be limited to compensation for the costs the bidder has incurred in making a bid."

Firstly, NCGB proposes that the board of the target company should ensure that any transaction agreements entered into are publicly disclosed in full as quickly as possible. This will give the market the opportunity to evaluate any such agreement in advance of the subsequent publication of the offer

document. In addition, the existence of a recommendation for public disclosure can be expected to encourage both the bidder and the board of the target company to focus their attention on the content of a transaction agreement. The public disclosure of transaction agreements will be in addition to the disclosure of the information that the target company must provide and should provide to shareholders in respect of a bid for the company's shares.

Secondly, NCGB proposes to include the current commentary on no shop and break fee provisions in the wording of the recommendation itself. This will impose a duty on the company to justify why any such provisions are included in a transaction agreement.

NCGB proposes adding the following wording to Section 14:

> "The board of directors should ensure that agreements entered into with the bidder on making and carrying out the bid are publicly disclosed as quickly as possible."

and

> "Any agreement with the bidder that acts to limit the company's ability to arrange other bids for the company's shares should only be entered into where it is self-evident that such an agreement is in the common interest of the company and its shareholders. This provision shall also apply to any agreement on the payment of financial compensation to the bidder if the bid does not proceed. Any financial compensation should be limited to the costs the bidder has incurred in making the bid."

NCGB proposes that equivalent changes should be made to the wording of the commentary on page 53.

NCGB also proposes a change to the wording of Section 14, third paragraph on not seeking to "hinder or obstruct" takeover bids. The Code currently stipulates that this should not be done unless there are "particular reasons". NCGB is of the view that the Code should be more categorical in this respect, and accordingly proposes the following wording:

> "The board of directors should not seek to hinder or obstruct take-over bids for the company's activities or shares ~~unless there are particular reasons for this~~".

NCGB proposes that equivalent changes should be made to the wording of the commentary on page 50.

7. Oslo Børs Code of Practice on the Reporting of IR Information (Section 13)

In addition to the changes to the sections and commentary proposed above, NCGB proposes to amend the footnote to Section 13.

Oslo Børs, in collaboration with the Norwegian Investor Relations Association, has issued a "Code of Practice for Reporting of IR Information", which addresses issues including the language used for reporting, publication of interim reports, publication of information outside exchange trading hours, and the information to be provided on the company website. In addition, Oslo Børs has issued recommendations on the information that companies should provide on their websites concerning legal provisions of relevance to investors. These recommendations and the IR code of practice are included in a brochure titled "Information from the company to investors and other interested parties".

The footnotes to the Code of Practice for Corporate Governance currently refer to the guidelines for additional information issued by the Norwegian Society of Financial Analysts in 2002.

NCGB proposes that this reference in the footnotes is replaced by a reference to the IR code of practice and recommendations mentioned above.

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Consultation Parties:

All companies listed on Oslo Børs and Oslo Axess
Ministry of Finance Ministry of Justice and Public Security
Ministry of Trade and Industry
Financial Supervisory Authority of Norway
Norwegian Competition Authority
Norwegian Shareholders Association
Arntzen de Besche advokatfirma
BAHR advokatfirma
BDO
Brønnøysund Register Centre
CLP advokatfirma
Deloitte
Norwegian Bar Association
Norwegian Institute of Public Accountants
Law Faculty, University of Bergen
Law Faculty, University of Oslo
Law Faculty, University of Tromsø
DLA Piper advokatfirma
Institutional Investor Forum
Ernst & Young
Finance Norway
Folketrygdfondet
Norwegian School of Management
Haavind advokatfirma
Enterprise Federation of Norway
Institutional Shareholder Services Inc
Kluge advokatfirma
KPMG
Norges Bank
Norges Bank Investment Management
Norwegian Securities Dealers Association
Norwegian School of Economics and Business Administration
Institute of Internal Auditors Norway
Norwegian Shipowners' Association
Norwegian Investors Forum
Norwegian Investor Relations Association
Norsk Tillitsmann ASA
Norwegian Venture Capital Association
Norwegian Society of Financial analysts
Næringslivets Aksjemarkedsutvalg
Confederation of Norwegian Enterprise
Oslo Børs ASA
Norwegian Association of Private Pension Funds
PricewaterhouseCoopers
Schjødt advokatfirma
Selmer advokatfirma
Simonsen advokatfirma
Steenstrup Stordrange advokatfirma
Norwegian Institute of Directors
Thommessen advokatfirma
University of Agder
Norwegian Mutual Fund Association
Verdipapirsentralen ASA
Wiersholm advokatfirma
Wikborg, Rein advokatfirma

Norwegian National Authority for Investigation and Prosecution of Economic and Environmental Crime