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## Revisions to the Code of corporate governance in Sweden

Norges Bank Investment Management ("**NBIM**") appreciates the opportunity to provide our perspectives on the revised Swedish Corporate Governance Code ("**The Code**"). NBIM is the investment management division of the Norwegian Central Bank (Norges Bank) and is responsible for investing the Norwegian Government Pension Fund Global ("**GPF**G"). At 30 June 2015, the fund was invested in assets of NOK 6,896 billion (SEK 7,241 billion) of which approximately SEK 97 billion was invested in equity of more than 170 Swedish listed companies.

We commend the Swedish Corporate Governance Board ("**Kollegiet**") for its systematic efforts to improve and update the code. Expanding on law, regulation and listing rules, the Code is helpful in describing and developing best practice. At the same time, it provides flexibility by the application of the 'comply or explain' concept.

Below, we provide comments and suggestions regarding:

- The description of the model of corporate governance and the typical ownership structure
- The voting on individual board candidates and the disclosure of vote tallies
- The strengthening of the shareholder model by removing board members from the nomination committee
- The encouragement of independent board members with deep industry knowledge
- The translation of shareholder meeting material into English

### **The description of the Swedish model of corporate governance**

We find it useful that the Code aims to explain the framework for corporate governance in Sweden. As a shareholder in more than 70 national stock markets globally, we appreciate the effort to compare corporate governance with other markets.

The Code describes the typical ownership structure of listed companies ("**II. 1 Ågarrollen**") as follows:

*"Ownership structure on the Swedish stock market differs significantly from that in countries such as the United Kingdom or the United States. While the majority of listed companies in those countries have a very diverse ownership structure, ownership in Sweden is often concentrated to single or small*

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*numbers of major shareholders, as is the case in many continental European countries.”*

It continues by describing how the ownership structure is of relevance to corporate governance:

*“Swedish society takes a positive view of major shareholders taking particular responsibility for companies by using seats on boards of directors to actively influence governance.”*

Finally, the Code points out («ll. 3 Styrelse”, last paragraph) how, on this basis, it is

*“possible for major shareholders of Swedish companies to appoint a majority of members with whom they have close ties”.*

We agree with Kollegiet that differences in ownership structure is of clear relevance to understanding local corporate governance. However, in Sweden, we find that the economic ownership of listed companies is relatively dispersed in a European context. Numbers indicate that the average concentration of economic ownership in Sweden, based on the consolidated holdings of the five largest shareholders in each company, is markedly lower in Sweden than the average in Continental Europe, and closer to and only slightly higher than levels in the United Kingdom.

Our analysis indicates, on the other hand, that a generally high level of voting-right concentration characterizes the Swedish market. The concentration of votes among the top five vote holders is higher in Sweden than in both Continental Europe and the United Kingdom. The disparity between ownership concentration and vote concentration is particularly strong for Sweden if we look at the largest Swedish companies and compare those to companies of similar size elsewhere in Europe.

The same pattern of a relatively open ownership structure and tighter vote concentration compared to Europe can be found if we instead compare the three largest holders of shares and votes, or the single largest holder.

These findings indicate how dominant owners in Sweden would often not be able to control companies just by virtue of their economic share of the equity. The bolstering of control by the usage of vote differentiation is what makes current levels of control possible.

There is a possibility that the ownership-vote disparity is self-perpetuating. Perpetuation may be effected through the prerogative of the board to initiate the terms of capital events, such as share issuance and buy-backs in the various share classes, conversion rights between the classes, acquisition and disposition of treasury shares, and the design of corporate transactions with regard to the balance between share classes.

As we revert to below, the particular Swedish measures of corporate governance are commendable as they rightly facilitate shareholder participation whereas the objective should not be undue consolidation of control. We suggest that Kollegiet adjusts the explanation of the distinction of the Swedish market to portray the relatively low ownership concentration in the European context and outsized control rights enjoyed and guarded by some large shareholders.

### **Board election**

The nomination committee (“Valberedning”) is a cornerstone in the Swedish corporate governance framework. What differentiates Swedish nomination processes is the way large-shareholder influence over nomination is *institutionalised* through the nomination committee. Most advanced markets apply nomination committees, but these are usually subcommittees of the incumbent board. Such



nomination subcommittees increasingly apply structured processes, draw on board evaluation, and are required to explain their considerations to the shareholder meeting. Involvement of major owners is not entirely unique to Sweden. Across companies in most markets, large owners, if there are any, will be permitted to exert influence over the nomination process.

The institutionalisation of the nomination process in Sweden, however, entails a number of advantages from the point of view of shareholders in general. The process leads to more transparency on the process, including disclosure of which shareholders are involved. In the case of differences of opinion between the largest shareholders, the nomination committee is still open for the different parties. We believe the explicit involvement of shareholders in the nomination process may give new board members a clearer understanding that they have a mandate from shareholders, rather than from previous board members. Finally, as a principled view, it is preferable that the recommendation for board composition comes from a body that is separate from the incumbent board, due to the obvious conflicts of interests when board members in other markets issue recommendations on their own future.

We would therefore suggest that Kollegiet seeks further refinement of the board appointment process, with an eye to exploiting the above advantages. We will below state some recommendations in this regard.

#### **Election procedure for board members**

The Code has a section called "III. 2 Appointment and remuneration of the board and statutory auditor". However, this Code does not discuss the actual method for election of board members by the shareholder meeting. We believe Kollegiet should introduce language on the election method, as this is currently a matter of some concern among international shareholders.

We acknowledge that voting at the shareholder meeting is predominantly a matter of approvals; it is usually not the role of the meeting to choose between alternatives. This is also the case for board elections, and in this respect, the Swedish market is not different from other markets. However, even when the approval by a majority is expected, the right for shareholders to register support or discontent should be respected. The number of shares that did not vote for approval of an individual board candidate should be seen as information that should be established and disclosed to all shareholders. On this issue, we believe that Sweden should now come in-line with most other advanced markets, where an individual vote and count for each board candidate – new as well as incumbent – is required. Companies should facilitate such candidate-by-candidate voting and counting, and a recommendation to this effect should be introduced in the Swedish Code, even if voting on individual candidates is not currently required by the law.

In our view, the new footnote no. 2 (under "II. 2") should be avoided.<sup>1</sup> We believe most foreign shareholders are aware that a shareholder can request separate voting on each board candidate. That is, however, not the issue of concern, as we explain below.

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<sup>1</sup> The footnote reads as follows: "The Companies Act states that the members who receive the most votes are regarded as elected. This means that there is no majority requirement, and that a vote against has the same weight as an abstention. A common misunderstanding is that the Board must be elected as a single unit at the shareholders' meeting. Even if there is only one proposal presented, the Companies Act gives each shareholder the right to propose its own candidates and to demand a vote on each of the proposed candidates. The latter also applies to discharge of liability, which under the Companies Act is determined individually for each member of the board and the chief executive officer."



Most foreign institutional shareholders must vote their shares by issuing vote instructions to a proxy who represents investors at the meeting, as in the most cases investors themselves are not able to attend each meeting. In the notice of the general meeting, Swedish companies generally present the election of board members as one voting item. At the meeting the election of board members is usually also treated as one voting item. On this basis, the proxy will collect vote instructions from investors on a one-item basis, as this is the expected procedure ex ante.

The ability for an individual shareholder to request that the shareholder meeting votes candidate-by-candidate does not solve this problem. Even if a request has been filed at the time proxy vote instructions have to be issued, shareholders and their proxies will usually not know whether the voting procedure will be amended for this meeting because of the request. This procedural uncertainty does not provide for candidate-by-candidate vote instructions, as the proxy-voting agent will not know whether such instructions can be implemented at the meeting. Should the meeting actually vote candidate-by-candidate following a request, most shareholders and their proxy voting agents will therefore be unprepared to take part in individual voting. Hence, the right to request individual voting at the individual meeting does not address the system failure to allow proxy-voting shareholders to differentiate their votes between individuals.

We are confident that as soon as most companies declare they will start practicing voting candidate by candidate at their shareholder meetings, the custodian banks will immediately amend their proxy procedures accordingly, allowing each proxy-voting shareholder the opportunity to give vote instructions candidate by candidate.

International shareholders generally see voting on individual candidates as best practice even if there are no excess candidates, for reasons such as the ones we mention above. Bundled elections is today routine or common in only a few markets, notably Brazil, Chile, Colombia, Finland, Greece, Indonesia, Italy, Luxembourg, Mexico, South Korea, Sweden and Turkey. However, most advanced markets facilitate voting candidate by candidate. Our experience in the majority of advanced markets where individual counting is common is that boards, nomination committees and shareholders take note of the individualised vote tally.

The common Swedish practice of effectively bundled board elections disregards the international efforts to ease cross-border voting and provide fair voting rights by proxy. The system unfairly advantages those shareholders who are able to be present in the room. Diversified institutional investors hold stocks in hundreds or thousands of companies and hence need to vote by proxy as they cannot attend each shareholder meeting in person.

We have elaborated our considerations on this topic in a position paper called "Individual vote count in board elections", which we have taken the liberty of attaching to this letter.

In summary, we would suggest that Kollegiet recommends voting on each individual candidate and the subsequent disclosure of the individual vote tally as routine practice for Swedish companies. This reform will be interpreted as increased board accountability in Sweden, and it will give nomination committees tangible feedback.

#### **Composition of the nomination committee**

Kollegiet has proposed the deletion of the restriction that only one board member on the nomination committee can be affiliated with a certain large shareholder (section III, paragraph 2.4). Kollegiet states that the stipulation is technically complicated and of limited utility.



For the nomination committee to have legitimacy we regard it as important that it is not unduly dominated by neither incumbent board members nor one large shareholder. One important advantage of the Swedish nomination committee is the explicit participation of shareholders, as discussed above. Principally, we would suggest that Kollegiet strengthens this positive feature by recommending that *no* representatives of the incumbent board should be members of the nomination committee. The board chair and other board members should still be invited to the committee as seen relevant by the committee itself. However, they should not be accountable for the recommendations that the committee makes.

We recommend against the proposed deletion and would suggest that a limit of one board member on the committee is set if board representation is to continue despite our proposal in the paragraph above.

Kollegiet asks about views on a new requirement that nomination committee candidates prior to accepting the appointment should consider whether conflicts of interest exist, for instance whether he or she is involved with a competitor. We support this.

#### **Composition of the board**

We believe Kollegiet should consider whether the existing requirement for just two board members independent of both management and major shareholders is sufficient. Compared to other advanced stock markets, the Swedish independence requirement is today towards the lower end, and in our view insufficient. NBIM shares the general view among large institutional investors internationally that the majority of shareholder elected board members should be independent, unless the company is controlled. In that case, at least a third should be independent.

While one should accept and expect shareholders holding a majority of the equity to exercise a certain level of control through the board composition, this should not be the case when a shareholder or shareholder group does not own a majority of the equity. In the Swedish context, we would expect shareholders with controlling voting power to influence board composition strongly. However, we see no reason why such shareholders should in addition use their influence to populate boards with a majority of board members that are not independent of them, if those shareholders do not also muster a majority of the equity capital.

Separately, the board members who qualify as independent of both management and major shareholders should between them have sufficient business specific knowledge to exercise effective monitoring of the performance and dealings of management. Usually, this would require that several such board members have senior-level work experience from the same industry. We are aware that company law already requires one of the independent members to have accounting or auditing competencies, because the audit committee must have at least one such member. We would suggest that Kollegiet considers how to introduce new language to the effect of encouraging deep industry knowledge among the independent board members.

#### **Translation of the shareholder meeting voting material and minutes**

Kollegiet considers (in III 1.4) changes to the requirement on translation of voting material and AGM minutes. We think any company listing in Sweden should accept the international nature of capital markets. Hence, we believe that all companies should provide an English language version of all reported or filed material, including all written material for the shareholder meeting and its minutes.

Importantly, all such English versions should be available in full at the same time as any Swedish-language versions. Any deviation from this principle amounts to information discrimination.



In the case the nomination committee has non-Swedish speaking members, all its internal deliberations and documentation should be held in English.

We would like to thank you for considering our perspectives, and remain at your disposal should you like to explore any of these issues further.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'P. Johnsen'.

Petter Johnsen  
CIO Equity Strategies

A handwritten signature in blue ink, appearing to read 'Ola Peter Krohn Gjessing'.

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Enclosure: NBIM Position Paper: Individual vote count in board elections