european corporate governance institute

Directors' Remuneration in Listed Companies

FINLAND*

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* The information and opinions included in this document are not intended to provide legal advice, and should not be relied on or treated as a substitute for specific advice concerning individual situations. The law, regulation and best practices are stated as they stood at 30 June 2003. **Please note that there are changes in Finnish best practices as of December 2003. The changes have been included in the Report.**

Questionnaire

Answers to this questionnaire should be given from the perspective of provisions included in national laws, regulations and exchange rules, and of best practices as recommended by either official reports or corporate governance codes.

1. General

1.1 Please indicate, as a general reference, the laws, case law, regulations, exchange rules and best practices concerning directors' remuneration in your country with respect to listed companies. Please indicate where these provisions (such as, for example, exchange rules) apply only to domestically-incorporated companies.

Apply only to domestically-incorporated companies:

- Chapter 8 § 11 a of the Companies Act, Chapter 8 § 1 of the Company Act interpreted in the light of § 11 a (Management of a company). Chapter 4 (Raising the share capital);
- Supreme Court decision 2002:73, Supreme Court decision 1998:136 (held e.g. that the contractual relationship must be distinguished from the company law relationship, meaning that the remuneration can be based either on company law or contract);
- Chapter 2 § 8 of the Accounting Ordinance (disclosure);
- The recommendation of the Ministry of Trade and Industry on corporate governance in state-owned companies, 13 November 2000.

Apply to all companies whose securities are publicly traded in Finland or whose securities are issued to the public in Finland:

- Chapter 2 § 5 of the Regulation of the Ministry of Finance on the regular duty of disclosure of issuer of securities, 538/2002 (disclosure);
- Section 2.3.3 of the Instructions of the Accounting Board concerning the Regulation of the Ministry of Finance on the regular duty of disclosure of issuer of securities, 29.10.2002 (disclosure);
- Chapter 3 § 12 of the Regulation of the Ministry of Finance on listing particulars, 539/2002 (disclosure);
- Chapter 3 § 12 of the Regulation of the Ministry of Finance on the prospectuses, 540/2002 (disclosure);
- The rules of the Helsinki Stock Exchange (chapter 5; no material requirements beyond the legislation);
- The Corporate Governance Recommendation for Listed Companies (hereafter "Recommendation"), December 2003, proposed by a working group of experts appointed by HEX Plc, the Central Chamber of Commerce of Finland (Keskuskauppakamari) and the Confederation of Finnish Industry and Employers (Teollisuuden ja Työnantajien Keskusliitto) and. The guidelines are recommended as best practice by the Helsinki Stock Exchanges and enter into force on 1 July 2004.

1.2 As to best practices, please specify whether they are described in either a private (voluntary or non-statutory) code or other official report, and whether a "comply or explain" principle is applicable to compliance with the relevant provisions by listed

companies. Where the "comply or explain" principle applies, please indicate, where such evidence is available, whether companies generally comply with best practices.

Private
The above mentioned Recommendation has reviewed the corporate governance recommendation for listed companies issued by the Central Chamber of Commerce of Finland and the Confederation of Finnish Industry and Employers in the 1997, not any more up to date and due to that quite ineffective. Since the corporate governance for listed companies in Finland is primarily based on compelling legislation and self-regulation, the Recommendation is designed to complement the statutory procedures (Recommendation 1.2).
The Recommendation has been prepared in accordance with the "comply or explain" principle. The company must give information on compliance of the Recommendation both in its annual report and on its website (Recommendation 1.4).

Official report
The recommendation of the Ministry of Trade and Industry on corporate governance in state-owned companies (13 November 2000): the "comply or explain" principle does not apply.

1.3 Please describe in summary: the institutional structure for adopting executive remuneration rules or best practice codes; and any major proposals for reform concerning directors' remuneration.

See 1.2 about the present state of play concerning rules and best practices.

Legislation
The remuneration rules are based on the Companies Act, while the disclosure requirements are included into different regulation mentioned above as the Accounting Ordinance and several regulations of the Ministry of Finance based on the Securities Market Act.
Currently, the Ministry of Justice is working on a comprehensive amendment of the Companies Act. The disclosure issues are not, at the moment, under special revision.

2. Disclosure

2.1 Are listed companies required to publish a remuneration report, indicating the details of the compensation paid to the members of the Board of Directors?
How often must it be published and where is it retrievable?

To make public a separate remuneration report is neither required nor recommended. Chapter 2 § 8 of the Accounting Ordinance and Chapter 2 § 5 of the Regulation of the Ministry of Finance (538/2002) set out that compensation paid to the Board must be disclosed in the annual accounts in the way described in answer 2.3. Also as to best practices please see 2.3.

2.2 Must these reports be submitted, or are recommended to be, to a Securities Market Regulator or to a public authority responsible for collecting these documents?

No.

2.3 What information on directors' remuneration, individually and collectively, and on the remuneration committee, must be included, or is recommended to be included as

best practice, in the financial reports? Please include in your answer any specific requirements which apply to particular elements of remuneration, such as stock options, bonuses, and termination payments.

The Accounting Ordinance applicable to all companies (including listed companies)
The following information must be given concerning members of the board of directors collectively:
- salaries and other compensation for these duties;
- the total amount of loans granted to them, with indications of the interest rates and other main conditions;
- the total amount and main contents of guarantees and contingent liabilities granted by a company
- pension commitments related to these duties.

The Regulation of the Ministry of Finance (538/2002) applicable to listed companies
The following information must be given concerning members of the board of directors collectively:
- salaries and other compensations;
- benefits in kind.

The following information collectively with corresponding bodies as the supervisory board, managing director etc:
- the total amount of holdings of the company's shares and convertible debt instruments, option loans and stock options issued by the company as well as of the portion of voting rights and share capital which they may acquire under these convertible debt instruments, option loans and warrants.

The Recommendation
The Recommendation uses the terms "describe" or "report" to describe the dissemination of information to shareholders. Unless otherwise provided, the information shall in all such cases be disclosed at least in the annual report and on the Internet website of the company. If the company does not issue an annual report, the information must be given in connection with the notes to the financial statements.
The Recommendation states that the company shall:
(i) report the fees and other benefits of the directors for their board and committee work during the reporting year;
(ii) report the number of shares and share-related rights granted to the directors in compensation during the reporting year;
(iii) describe the criteria and decision-making procedure concerning the compensation system covering the managing director and other executives;
(iv) report the economic benefits based on the service contracts of the managing director and a full-time chairman of the board:
  - salaries and other benefits granted during the reporting year;
  - shares and share-related rights granted by way of compensation;
  - retirement age and criteria for determination of pension;
  - terms and conditions of the period of notice, salary for the period of notice and other possible compensation payable on the basis of termination
(v) as to the biographical details of directors, report the holdings and rights based on a share-related compensation system of the company (Recommendation 43, 46, 47, 48 and 19).

2.4 Is timely disclosure required with respect to stock options, their vesting, exercise, and the sale of the relevant shares to third parties?

See above 2.3 requirements relating to the board. The disclosure requirements concerning stock options and own shares generally are defined in detail in legislation.

2.5 What are the rules on disclosure of share transactions executed by the company's insiders (such as directors, officers, auditors, etc)?

The disclosure rules that apply to directors as other shareholders are included in the Securities Markets Act (Chapter 2 Section 9). They must disclose information of their shareholdings without undue delay if their portions exceeds or falls below certain threshold starting from one-twentieth and ending up to two-third. Furthermore, in the Chapter 5 of the Securities Markets Act there are rules about the registers of insider holdings and about the duty to declare information to the register.
Financial Supervision Authority has issued regulation on declaration of insider holdings and on registers. In addition the companies must comply with the Guidelines for Insiders issued by the Helsinki Exchanges and describe its essential insider administration procedures (Recommendation 52).

2.6 What information on directors' remuneration must be included in public offer prospectuses and listing particulars?

Following information concerning the board is required in both public offer prospectuses and listing particulars based on regulation of the Ministry of Finance (see 1):
- total salaries and remuneration paid and benefits in kind collectively;
- total number of shares, convertible debt securities, option loans and option rights issued by a company and owned by the board members and corresponding persons;
- total of loans or guarantees granted by the issuer to the board members and corresponding persons;
- a description of the incentive schemes or other corresponding arrangements involving issues directed or to be directed to the board or other in legislation determined bodies.

3. Remuneration of The Board of Directors

3.1 Who fixes the board of directors' remuneration? What are the relevant procedures? (In two-tier systems, please refer to the supervisory board.)

The company has a supervisory board:
Remuneration paid to members of the board in that capacity: the general meeting or the supervisory board unless otherwise stipulated in the articles of association.
Remuneration paid to members of the board in the capacity of employees: the board, the managing director, any other person having authority depending on the seniority of the employee in question.
The Recommendation provides that company shall describe the duties and the operation principles of the supervisory board as well as the criteria for compensation of the members of the supervisory board (Recommendation 6).
In addition, the articles of association may set out that the supervisory board will decide on the benefits of senior management. Some members of the supervisory board and members of the board may in practice belong to senior management.

Right to subscribe for new shares (share options):

The general meeting of shareholders will always decide on the right to subscribe for new shares.

3.2 Are there provisions and/or practices as to the amount of the remuneration and its distribution (for example, as to whether distribution should be proportionate) among board members? What types of remuneration are allowed?

There are no rules on proportionality. However, measures which are likely to cause unjust enrichment to a shareholder or a third person at the cost of the company or another shareholder are generally invalid under Chapter 8 § 14 and Chapter 9 § 16 of the Company Act.
There are no rules on the types of remuneration allowed. As to best practice, Recommendation states that the shareholdings of the directors can be increased by paying the fees or part of the fees for board and committee work in the form of shares of the company (Recommendation 44).

3.3 Are personal loans to the company's directors and officers allowed?

Yes. Loans to persons belonging to the inner circle as defined in the Companies Act are as a rule permitted under Chapter 12 § 7 provided that the loans are granted within the limits of the distributable assets (profits) of the company and against a safeguarding collateral.

4. Executive Directors' Remuneration

4.1 Who fixes the executive directors' remuneration? What are the relevant procedures? Are shareholders required to approve directors' remuneration, the remuneration policy, or the remuneration report (see question 2) on an annual or other basis?
(In two-tier systems, please refer to the management board.)

The company does not have a supervisory board:
Remuneration paid to members of the board in that capacity: the general meeting who also elects at least the majority of the members to the board of directors. The general practice has been that the general meeting decides on the remuneration to the board members even though it is not stipulated in the Companies Act. The principle is included in working documents of the Companies Act.
Remuneration paid to members of the board in the capacity of employees: the board, the managing director, any other person having authority depending on the seniority of the employee in question.
Finnish company law does not distinguish between executive members of the board of directors and non-executive members. However, Recommendation stresses that the compensation committee is designed to improve the effective handling of matters relating primarily to the appointment and compensation of the managing director and other executives (Recommendation 34).

4.2 Is the board required, or recommended as best practice, to create a remuneration committee?

The Recommendation provides that the board may establish a compensation committee to improve the transparency and systematic functioning of the compensation systems of the company. The company reports the composition of the committee (Recommendation 34 and 26).

If yes, please specify:

(i) **the committee's composition (if independent directors should be appointed to this committee, please give the relevant definition and indicate whether any special procedures apply to the appointment of independent non-executive directors)**
The board elects from among the directors the members and the chairman of the committee. The managing director and other executives must not be members of the compensation committee. The independency[1] of directors is not specifically recommended but should be assessed and reported. (Recommendation 35, 25 and 18[1]).

(ii) **the committee's competences and which company body it reports to**
The board defines the duties of the compensation committee, which regularly reports on its work to the board (Recommendation 36 and 22).

(iii) **how the committee operates**
The board approves a written charter for the committee's work and describes its essential content (Recommendation 23).

4.3 Which types of remuneration are permitted?

As a rule, all of these types of remuneration may be permitted under some circumstances. One must nevertheless take into account the basis of remuneration (e.g. remuneration for board membership v remuneration on the basis of service contract), the party granting remuneration (e.g. a shareholder or a third party v the company) and the type of remuneration (e.g. rights to subscribe for new shares v money).
In theory, discounted stock options may be used under some circumstances. However, the pre-emptive subscription rights of existing shareholders and the requirement of a weighty financial reason to deviate from that right (see below) and on the other hand, the general principles of company law protecting shareholders and a company from unjust benefits permit the use of discounted stock options only rarely. According to one view, discounted stock options may be used for the benefit of the personnel but discounted stock options will be very difficult to apply in practice.

In answering, please consider each of the following:

(a) **bonuses**

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[1] A director is not independent of the company if he (i) has an employment relationship with, or holds a position in, the company; (ii) has had an employment relationship with, or held a position in, the company during the last three years prior to the inception of the board membership; (iii) receives from the company or from a member of its operative management not insignificant compensation for services or other advice not connected with the duties of the board, e.g. if the director works on consulting assignments for the company; (iv) belongs to the operative management of another company, and the two companies have a customer, supplier or cooperation relationship significant to the other company; (v) belongs to the operative management of another company whose director is a member of the operative management in the first company (interlocking control relationship). In addition, the board can on the basis of its overall evaluation determine that a director is not independent of the company if he (vi) participates in a performance-based or share-related compensation system of the company. The financial significance of the compensation system shall be taken into account; or (vii) the company is aware of other factors that may compromise the independence of the director and the directors ability to impartially represent all shareholders. Furthermore, a director is not independent of a significant shareholder of the company if he (viii) exercises dominant influence such as referred to in Chapter 1, Section 3 of the Companies Act1, in the company, or has a relationship such as referred to in sub-sections a) - b) above to a party who exercises dominant influence in the company; or (ix) is a significant shareholder of, or has a relationship such as referred to in sub-sections a) – b) above to, a significant shareholder of the company. Significant shareholder means a shareholder who holds at least 10 % of all the shares or of the aggregate votes in the company.

(b) stock options, including discounted stock options
(c) stock grants
(d) profit sharing
(e) benefits in kind

4.4 Are there specific rules, including shareholder approval requirements, as to these different types of remuneration?

The use of stock options and stock grants are not possible without the consent of the general meeting of the shareholders.
According to Chapter 4 § 2 of the Companies Act, when stock options are issued the existing shareholders shall have the pre-emptive subscription rights to stock options and it is only the general meeting of the shareholders who has right to decide on the deviation from that right. In addition, the decision on deviation shall be justified of a weighty financial reason of the company. The general meeting may authorise the board to decide on granting stock options providing that it is not a question of remuneration of board.
To grant stocks is very difficult for the company due to the limitations on the purchase and sale of the company's own shares according to the provisions of Chapter 7 in the Companies Act.

4.5 Are there any restrictions on how payments are made?

No.

4.6 Are there any specific requirements for termination payments made on loss of office, whether through dismissal, retirement, on a takeover, or otherwise?

There are no such rules in the Company Act. Such rules may be based on contract.

4.7 Are there any specific requirements concerning directors' service contracts with respect to, for example, their duration and disclosure?

Not as such prior to the Recommendation. The service contracts might not contain clauses which do not comply with the Company Act or the articles of association. For example, the company might not validly agree on a term of a board member exceeding the maximum term set forth in the articles of association.
With the introduction of the new guidelines, the general recommendation is that the directors should be elected for a term of one year. The managing director's service terms and conditions are to be specified in writing in the managing director's service contract approved by the board. Moreover, the company discloses the biographical details and the holdings of the managing director (see 2.3) (Recommendation 12, 38, 39 and 48).

5. Non-executive Directors' Remuneration

5.1 Are non-executive directors separately paid for their participation in committees of the board of directors? Do any restrictions apply to the payment of non-executive directors' *via* stock options?

Finnish company law does not distinguish between executive directors and non-executive directors. However, the new Recommendation specifies that it is not recommended that a non-

executive director should participate in a share-related compensation system (Recommendation 45).

5.2 May a company make payments to non-executive directors, additional to their directors' fees, for services, such as legal or brokerage services, outside the usual scope of directors' duties?

Yes.