



C O R P O R A T E

G O V E R N A N C E

GUIDELINES

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SECOND EDITION

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1 INTRODUCTION

Increasing liberalisation of trade and commerce in recent years has also meant increasing freedom of action. Internationalisation of business operations has characterised this development and cross-border connections between companies have increased greatly. Iceland has not been untouched by this process. Icelandic companies have demonstrated their ability to undertake new projects both within Iceland and abroad, thereby contributing to the country's increased welfare. Increased freedom carries with it greater responsibility; companies have to respect their shareholders and pay careful attention to relations with customers and society at large. The Icelandic business community is determined to demonstrate that it can shoulder this increased responsibility. One effective means of doing this is for businesses to take the initiative themselves in adopting rules and procedures which reinforce their own corporate structure and increase trust between companies and the general public. Mutual trust between the public and the business community is a key to improving Iceland's competitiveness and standard of living. The introduction of



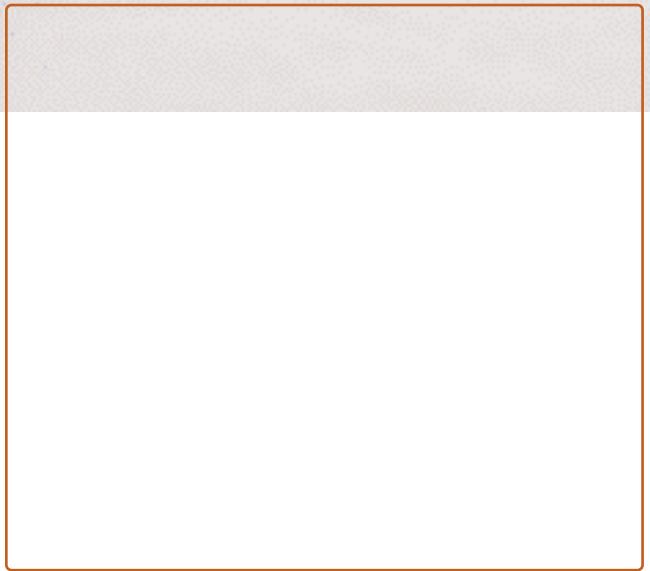
Guidelines on Corporate Governance in 2004 was a major step towards ensuring business credibility. Those Guidelines included provision for a review at the end of 2005, and the new Guidelines are the result of this revision. The Guidelines are aimed at providing companies with guidance on relations between shareholders, Boards of Directors, and management. They reflect international efforts to improve corporate governance in a new, globalised business environment. Many states, international organisations and business associations have, in recent years, drawn up corporate governance proposals and these issues have been the subject of considerable attention.

The Guidelines presented here should be suitable for public limited companies, whether officially listed on the Iceland Stock Exchange (ICEX) or not, as well as private limited companies and public corporations, as appropriate. Administrators of other companies or institutions can also make use of the guidelines, in whole or in part, as appropriate. Although the Guidelines are not mandatory, listed companies are required to take them into consideration, as provided for in Section 2.5.9 of the Rules for



Issuers of Securities Listed on the Iceland Stock Exchange. They are to follow the so-called "Comply or explain" rule, which states that if companies do not fully comply with these Guidelines they must explain any points of divergence and the grounds for such in their annual financial statements or annual reports.

The working group on corporate governance was comprised of the following members: Thordur Fridjonsson, President and CEO of ICEX, Chairman; Ari Edwald, managing director of the Confederation of Icelandic Employers; Erlendur Magnússon, managing director of Islandsbanki, dr. Gudfinna S. Bjarnadóttir, Rector of Reykjavik University; Olafur Nilsson, CPA, KPMG; Svanbjorn Thoroddsen, managing director of Straumur-Burdaras Investment Bank; Thorgeir Eyjolfsson, director of the Pension Fund of Commerce; and Thor Sigfusson, managing director of the Iceland Chamber of Commerce. David Sch. Thorsteinsson was project manager. Sigridur A. Andersen, legal council, and David Thorlaksson of the Chamber of Commerce also assisted the group.



2 DIRECTORS

As a company's ultimate authority between shareholders' meetings, the Board of Directors is entrusted with considerable responsibility. Its chief role, as provided for by law and the nature of the case, can be summarised as follows:

- The Board of Directors is to promote the company's success and supervise its management and overall operation.
- The Board, together with the managing director should take the initiative in formulating the company's strategy, both for the short term and the long term.
- The Board is responsible for always safeguarding the interests of all the company's shareholders, as Directors are not to act specifically in the interests of parties supporting their election to the Board.

Section 5.3 below includes a summary of the principal provisions of the Act on Public Limited Companies concerning a company's Board of Directors.

The following Guidelines on Boards of Directors and sub-committees are intended to outline best practices for Directors to follow in fulfilling their duties.

2.1 Duties

All persons elected as Directors must possess the necessary qualifications to be able to fulfil their duties as Directors and be able to devote the time required by such duties. It is important that Directors be aware of the obligations which their position entails.

To function effectively, a Board needs knowledge of the company's activities. A basic prerequisite for effective and successful Board work is for Directors to complement each other with varying expertise, qualifications and skills. Each Director must have sufficient time to devote to duties in the company's service. Directors must:

- have a good grasp of current laws and regulations applying to corporate operation and relevant activities, understand their role and whose interests they represent;
- understand the company's objectives and undertakings, as well as how they can conduct their work as Directors in order to contribute to achieving these objectives;
- have an understanding of the Board's function, have good judgment and insight;
- take independent decisions in each individual instance;
- ensure that internal checks and controls are in place, that the Board receives information to monitor operations and that decisions by the Board are implemented;
- verify that laws, regulations and rules are adhered to at all times;
- encourage positive staff morale.

2.2 Rules on Working Procedures

The Board must adopt written rules on working procedures, which specify the role of the Board and the implementation of its tasks.

The Rules of Procedure must describe the division of responsibilities among Directors and the relations between the Board, its Chairman and the managing director. The information provided in the Board's Rules of Procedures will also facilitate an assessment of its work by shareholders.

The Board's Rules of Procedure should deal with the following aspects:

- division of responsibilities among Directors;
 - duties of the Board and its Chairman;
 - the Board's sub-committees;
 - calling meetings, frequency of meetings, participants and formalities;
 - meeting documents;
 - minutes of meetings;
 - decision-making and voting;
 - obligations of confidentiality;
 - ineligibility;
 - relationship to other rules of the company;
-
- relationship with other rules as appropriate, such as FME and ICEX rules, cf. for instance the summary in Section 5.3.

The Chairman of the Board is responsible for ensuring that Directors perform their tasks effectively, which requires that a description of the duties and responsibilities of the Chairman be available, outlining how he/she is intended to perform these duties.

2.3 Information Disclosure to the Board

It is important that the Board receives regular information from the managing director to enable it to perform its duties. The manner in which such information disclosure shall be effected must be specified.

Directors need to receive information on financial matters, the company's development and its operations regularly to enable them to perform their duties. Furthermore, new Directors must be made thoroughly acquainted with the company.

Information provided to the Board by the managing directors must be made available in good time and in such format and quality as will enable the Board to perform its duties satisfactorily.

2.4 Evaluation of Performance

The Board should preferably assess regularly its own work, working methods and working procedures and the company's performance, with the assistance of external parties if appropriate.

Such performance assessment implies that the Board evaluates the strengths and weaknesses of its work and working methods and focus on those aspects of its governance it feels could be improved.

2.5 Independent Directors

Preferably the majority of the Directors should be independent of the company, cf. the definition in Section 2.6. Furthermore, at least two of the Directors should preferably be independent of major shareholders in the company.

It is the responsibility of the Board to supervise those responsible for the company's day-to-day operations. This makes it preferable for the majority of the Board to be independent of the company and for at least two Directors on a five-person Board to be independent of major shareholders in the company.

A major shareholder is any party controlling at least 10% of the company's total share capital, either singly or acting in concert with related parties.

2.6 Assessment of the Independence of Directors towards the Company

The Board itself shall assess whether a Director is independent of the company and give an account of its conclusion in the company's annual financial statements or annual report.

If the majority of Board members is not independent of the company, it is important that mention be made thereof in the annual report. A Director shall not be considered to be independent of the company:

- if he/she is or has been an employee of the company or group during the past three years;
- if he/she receives payment from the company, or its senior management, apart from remuneration received as a Director, e.g. as a consultant or contractor;
- if he/she has close family connections with any of the company's consultants, Directors or senior management;
- if he/she is a member of the senior management of another company, which does substantial business with the company;
- if he/she is a member of the senior management of a company where one of the company's senior managers serves as Director;
- if he/she does substantial business with, or has substantial business interests at stake, in the company;
- if he/she is included in a performance-linked remuneration system of the company;
- if the Board is aware of any other aspects where the interests of a Director could overlap significantly with those of the company.

Directors must provide personal information to facilitate the above-mentioned assessment by the Board and on any changes to their circumstances which could affect the Board's assessment as to whether or not they are independent. The company's annual financial statements or annual report should include the following information on Directors:

- name and date of birth;
- education;
- principal occupation;
- positions held;
- date of first election to the Board;
- other appointments;
- holdings in the company;
- options on the company's stocks;
- spouse.

3 SUB-COMMITTEES OF THE BOARDS

Effective organisation of the Board's work is a premise for its efficacy and for the operations of the company as a whole. Establishing sub-committees, which include one or more Directors as members, can improve working practices in those matters for which the Board is responsible. Directors working in such specialised committees can concentrate better on the tasks entrusted to them than when the Board meets in its entirety. It is important that sub-committees report regularly to the Board on the principal results of their work.

3.1 Establishment of sub-committees

To make the work of the Board more effective, it may be suitable to establish certain sub-committees of the Board. The Board shall appoint the Directors to take part in and chair the committees. The annual report should give an account of the members of each sub-committee.

It may be necessary to entrust the Board's sub-committees to examine specific aspects, in particular those concerning financial supervision and remuneration to managing directors and senior management. The Board must assess the need for such committees in accordance with the size and scope of the company and the composition of the Board.

A AUDIT COMMITTEE

A.1 Appointment of an Audit Committee

An Audit Committee should be appointed if the extent of the company's operations is such as to make it important to have surveillance and reporting on its financial affairs undergo a more detailed examination and analysis by a smaller group than the entire Board of Directors.

The Audit Committee should review financial data and the arrangements for information disclosure by management, thereby ensuring that the information obtained by the Board on the company's operations, financial situation and outlook give as clear a picture of the company's current position as possible.

Companies which have not already established such a committee must assess annually whether there is a need to do so.

A.2 Selection of committee members

The Audit Committee shall be comprised of at least three members, the majority of whom must be independent of the company. The Committee may be comprised of two members, however, in which case both of them must be independent of the company. Committee members must have the requisite experience and knowledge to carry out its work.

Since the task of the Audit Committee is to deal with financial issues, results and supervision of the same, all Committee members must have a thorough knowledge of accounting and preparation of financial statements.

A.3 Role

The Board shall define the role of the Audit Committee, taking into consideration the needs of the company.

The Committee's role should include the following:

- monitoring the company's financial position;
- evaluation of its internal surveillance and risk management;
- evaluation of management reporting on financial issues;
- assessment of whether all statutes and regulations are complied with;
- preparation of the election of the company's auditor;
- direct access to the company's auditor;
- evaluation of auditor's reports;
- assessment of other work carried out by the company's auditor.

B REMUNERATION COMMITTEE

B.1 Appointment of a Remuneration Committee

The Board may appoint a special Remuneration Committee, to negotiate with managing directors and other employees on salaries and terms of employment, if these parties also sit on the Board. Furthermore, such a Committee may draft company policy concerning performance linking of salaries and/or stock options in the company, as applicable.

A Remuneration Committee should be established in all instances where a managing director also sits on the Board of Directors, or if the Chairman of the Board or other Directors are also company employees.

B.2 Selection of committee members

The Remuneration Committee shall be comprised of three members, the majority of whom must be independent of the company.

The Committee may be comprised of two members, however, in which case both of them must be independent of the company.

Due to the nature of its work, neither a managing director nor other employee may serve on the Committee.

B.3 Role

The Board shall define the role of the Remuneration Committee.

The Remuneration Committee's duties and working methods shall be defined in a formal statement of duties provided to the Committee by the Board, which reflect the company's needs. The Committee's role should include the following:

- to negotiate with managing directors on salaries and other terms of employment;
- to negotiate with other employees who also sit on the Board on salaries and other terms of employment;
- to draft company remuneration policy, including performance-linking of salaries and options on the company's shares.

B.4 Stock option plans

The principal provisions of stock option plans should preferably be submitted to a shareholders' meeting for approval.

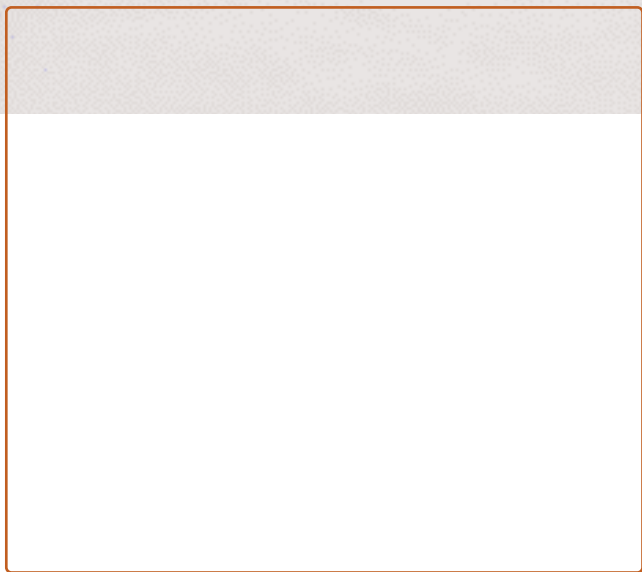
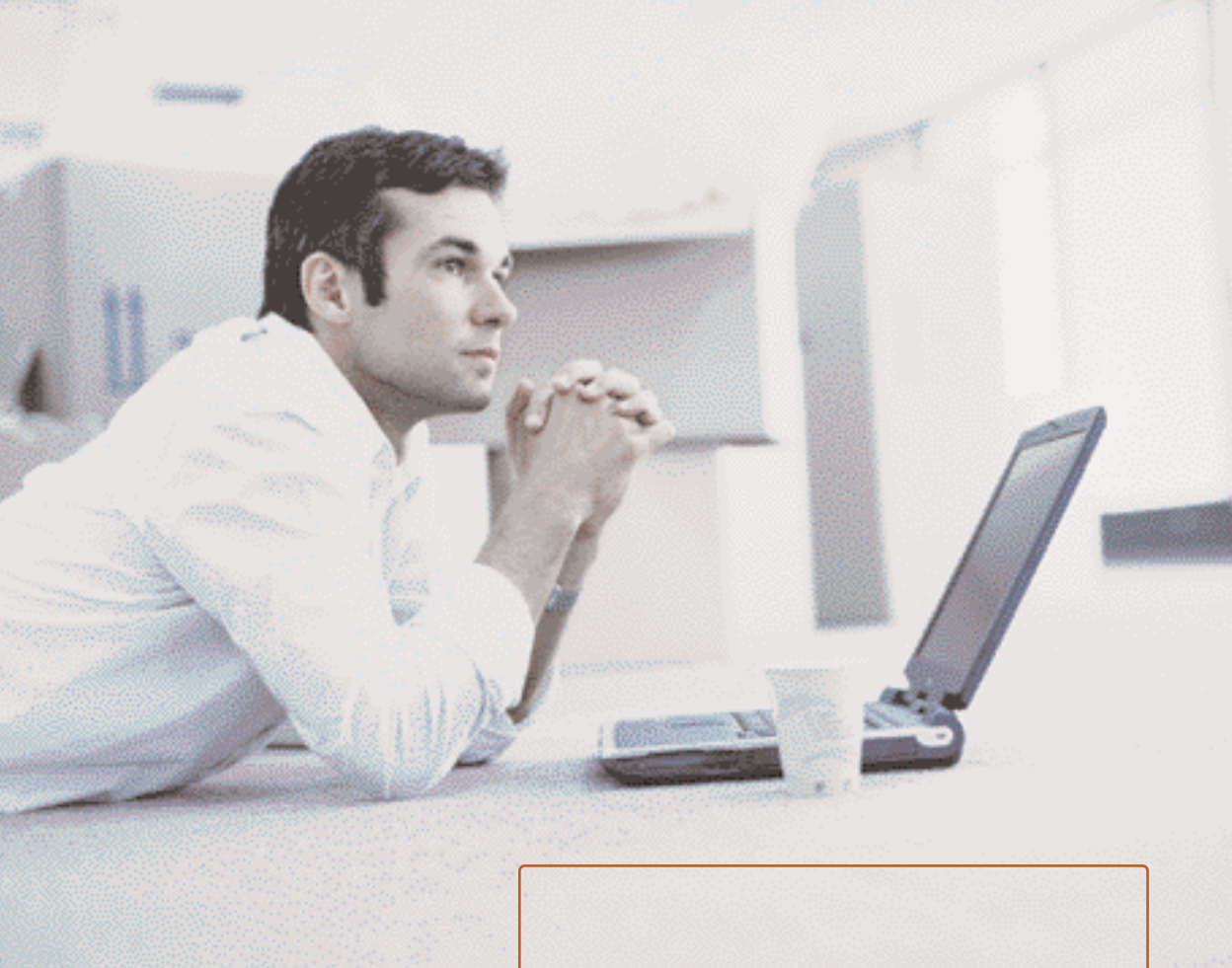
If it is company policy to conclude contracts with employees for call options on shares, or if they are sold shares with put options, the principal provisions of such contracts and/or plans should be submitted to a shareholders' meeting for approval. Principal provisions include, for instance, the total number of shares in the plan, the maximum duration of stock option contracts, the time during which employees may exercise their options, what reference was used to determine the purchase price, and the terms, if loans are involved; this does not mean contracts with individual employees or their amounts.

If a stock option plan also includes Directors, that portion of the stock option plan should be discussed specifically at a shareholders' meeting concurrent to discussion of remuneration to Directors.

4 REVISION OF GUIDELINES

These Guidelines should be reviewed regularly in light of experience.

It should be pointed out that there is no accepted international definition of good corporate governance, and therefore further discussion of the subject is to be expected. This makes it necessary to follow closely developments in this area, both in Iceland and abroad, and to review these Guidelines regularly.



5 ANNEX - SUMMARY OF RELATED RULES AND LEGISLATION

The Guidelines on Corporate Governance are somewhat briefer and simpler in content than the foreign rules upon which they were chiefly modelled. One of the reasons for this is that rules in other countries often include aspects which in Iceland are covered by the Rules for Issuers of Securities on the Iceland Stock Exchange Ltd. (ICEX Rules), which are available on the ICEX website, and Act No. 2/1995, on Public Limited Companies (Companies Act). The Guidelines of the Financial Supervisory Authority, available on www.fme.is, should also be mentioned. A brief summary of the relevant provisions of such rules is provided below. The ICEX Rules came into force on 1 January 2005 and the Companies' Act is considered to be fairly recent, and was last amended in 2003. They reflect, for the most part, the developments which have taken place in this area.

5.1 Remuneration to Management

Rules on Disclosure Requirements on Remuneration to Management are laid out in Section 2.5 of the ICEX Rules. This is also dealt with in Article 43 of the Financial Statements Act, No. 144/1994. The Companies Act does not deal with such disclosure requirements, but only states, in Article 79, that the "Annual General Meeting will decide upon the annual wages of Directors and Representative Committee members" (first paragraph) and that the "Board of Directors will decide upon the wages and terms of a Manager",

The previously mentioned section of the ICEX Rules places an obligation on the company to disclose information on the following points in its Annual Financial Statements:

- remuneration to managing directors and the Board of Directors and, if applicable, the remuneration to the same persons in companies in the same group, as well as examiners and representative committee members, cf. Sections 2.5.2 and 2.5.5. Mention must also be made of any extraordinary transactions concluded with these parties, cf. Sections 2.5.6 and 2.5.7 and the first paragraph of Article 43 of the Financial Statements Act, No. 144/1994, and of their shareholdings in the company, cf. Section 2.5.8.
- Information on the total remuneration of other managers and the number of managers, cf. Sections 2.5.3 and 2.5.5., and their total shareholdings in the company, cf. Section 2.5.8.
- Information on total payments to auditors, cf. Section 2.5.4.

5.2 Managing Director

The Companies' Act contains a variety of Rules concerning the managing director.

Role

- responsible for day-to-day operations in accordance with the specific instructions of the Board, cf. the second paragraph of Article 68;

- administers the company together with the Board, cf. the first paragraph of Article 68.

Eligibility

- General rules on eligibility are laid down in Article 66.
- may not be Chairman of the Board, cf. the first paragraph of Article 70;
- may not be on the Representative Committee, cf. the second paragraph of Article 73;
- may not take part in the preparation of an agreement where he/she has personal interests at stake, cf. Article 72.

Rights

- May demand that a meeting of the Board of Directors be held and has the right to speak and make proposals at meetings, cf. the second paragraph of Article 70, and may also have an opinion entered in the minutes of a meeting, cf. the third paragraph of Article 70;
- May represent the company, cf. Article 75;
- May demand that a shareholders' meeting be announced, cf. the second paragraph of Article 87;
- May institute legal proceedings on account of a decision by a shareholders' meeting, cf. the first paragraph of Article 96.

Duties

- Shall see to it that the company's accounts are kept properly and its assets securely handled, cf. the third paragraph of Article 68;
- shall disclose his/her shareholding in the company, cf. the first paragraph of Article 67;
- shall provide information on the annual financial statements at the AGM, if required, cf. the first paragraph of Article 91;
- shall explain to a shareholders' meeting changes which have occurred to the assets or liabilities if the company is to be divided up, cf. the second paragraph of Article 133.

Prohibitions

- May not abuse his/her position to deal in the company's shares, cf. the second paragraph of Article 67;
- May not do anything to acquire for any party undue interests at the expense of the company or its shareholders, cf. the first paragraph of Article 76;
- May not carry out illegal decisions, cf. the second paragraph of Article 76;
- May not borrow from the company, cf. the first paragraph of Article 104.

Responsibility

- Bears personal responsibility for ensuring that the company does not subscribe for its own shares when share capital is increased, cf. the third paragraph of Article 62;
- is liable to the company for damages should he/she cause it loss, cf. the first paragraph of Article 134;
- is liable to criminal prosecution if he/she does not comply with the Companies' Act, cf. Article 152.

5.3 Board of Directors

The Companies' Act contains a variety of Rules concerning a company's Board of Directors.

Role

- administers the company's affairs and sees to it that the company's organisation and activities are functioning properly, cf. the first sentence of the first paragraph of Article 68;
- directs the company, together with the managing director, cf. the second sentence of the first paragraph of Article 68;
- represents the company and has power to sign, cf. the first paragraph of Article 74.

Eligibility of Directors and the Board of Directors

- The majority of the Board must be comprised of persons other than the company's managing directors, cf. the second paragraph of Article 65;

- half of the Directors must be resident in Iceland or an EEA state, cf. the second paragraph of Article 66;
- must be legally and financially competent, cf. the first paragraph of Article 66;
- may not have received a criminal sentence in connection with business activities in the past three years, cf. the first paragraph of Article 66;
- may not take part in the preparation of an agreement where they have personal interests at stake, cf. Article 72;
- may not be on the Representative Committee, cf. the second paragraph of Article 73;
- A managing director of a company may not also be Chairman of the Board, cf. the first paragraph of Article 70;
- The Board shall have a quorum when a majority of the Directors attends a meeting, cf. the first paragraph of Article 71.

Rights

- May approve the netting of a claim arising from a subscription to share capital, cf. the second paragraph of Article 16;
- May bring suit to collect unpaid share capital or deliver the shares to other persons, cf. the second paragraph of Article 17;
- May approve the mortgaging of shares, unless otherwise provided for in Articles, cf. the second paragraph of Article 23;
- May decide, together with an owner holding at least 90% of share capital, that other shareholders shall be subject to mandatory redemption of their shares, cf. the first paragraph of Article 24;
- May decide that the company's shares shall be de-materialised, cf. the second paragraph of Article 27;
- May institute legal proceedings to invalidate lost share certificates, cf. the eighth paragraph of Article 27;
- May issue a provisional voucher if shares have not been fully paid up, cf. the first paragraph of Article 28;
- May make necessary amendments to Articles required by an increase in share capital, cf. the third paragraph of of Article 40 and the third

paragraph of Article 49, and share capital decrease, cf. the first paragraph of Article 54;

- May call upon parties to collect unclaimed bonus share certificates, and sell those then remaining uncollected, cf. Article 44;
- May delete a provision on a share capital increase from the Articles once the time limit for subscription to the increase has expired, cf. the third paragraph of Article 45;
- May approve a decrease in share capital, but only as authorised in Points 2 to 4 of the second paragraph of Article 51, cf. the third paragraph of Article 51;
- May grant authorisation to sign, cf. the fourth paragraph of Article 68;
- May in particular instances decide that the managing director does not have the right to speak and make motions at a Board meeting, cf. the second paragraph of Article 70;
- May make minor donations to charities, cf. the second paragraph of Article 103.

Duties

- Consideration shall compile a written report if the initial share capital is not in cash, cf. the second paragraph of Article 8;
- shall register the company with the Registrar, cf. the first paragraph of Article 14;
- shall inform pre-emptive rightholders of an announcement of an offer to purchase shares subject to pre-emptive rights, cf. the third paragraph of Article 22;
- shall see to it that amendments to share certificates are entered on them, cf. the seventh paragraph of Article 27;
- shall compile a share register, cf. the first paragraph of Article 30;
- shall give notice of a share capital increase, cf. the third paragraph of Article 40;
- shall inform a shareholders' meeting of purchase of own shares, cf. the second paragraph of Article 56;
- shall decrease share capital if own shares are not sold as required, cf. Article 61;

- shall hire a managing director, cf. the second paragraph of Article 65;
- must give notice of major actions taken by the managing director, cf. the second paragraph of Article 68;
- shall ensure sufficient supervision of accounting and handling of assets, cf. the third paragraph of Article 68;
- The Board of Directors of the parent company shall, when a group is formed, notify the Board of a subsidiary thereof and the Board of the subsidiary shall provide the necessary information, cf. the first paragraph of Article 69;
- shall elect a chairman, unless the Articles provide for a shareholders' meeting to do so, cf. the first paragraph of Article 70;
- shall adopt its own rules on working procedure, cf. the fourth paragraph of Article 70;
- shall call a shareholders' meeting within six months of such time as the company's equity has fallen below one-half of its share capital, cf. the fourth paragraph of Article 84;
- shall look after the announcement of a shareholders' meeting, cf. the first paragraph of Article 87;
- shall submit to the company's Annual General Meeting information on the company's annual financial statements, if required, cf. the first paragraph of Article 91;
- shall hand over the estate to bankruptcy proceedings, in such eventuality, cf. the first paragraph of Article 105;
- shall give notice of a merger, cf. Article 128;
- shall explain to a shareholders' meeting changes which have occurred to the assets or liabilities if the company is to be divided up, cf. the second paragraph of Article 133.

Prohibitions

- May not do anything to acquire for any party undue interests at the expense of the company or its shareholders, cf. the first paragraph of Article 76;
- May not carry out illegal decisions, cf. the second paragraph of Article 76.

5.4 Information Disclosure

No requirement is set in these Guidelines or by law obliging a company to have a website where it publishes specific information. The reason is that larger companies generally have websites and, secondly, that the Iceland Stock Exchange publishes all announcements on its news website, at www.icex.is. Chapter 2 of the ICEX Rules concerns information disclosure, which is of two types.

On-going disclosure requirements, cf. Section 2.2, apply when a company possesses information which has not been made public, which can have a significant impact on the price formation of its shares. Several examples are mentioned as illustrations, but the company must give notice of other similar events.

- Changes to the composition of the Board of Directors, or to its senior management or auditors, cf. Section 2.2.3;
- Employee stock option plans, cf. Section 2.2.4.
- Listing of the company on other stock exchanges, cf. Section 2.2.5.
- Changes to the company's financing, cf. Section 2.2.7.

On the other hand, there is regular information disclosure, cf. Sections 2.3 - 2.5, where the listing is exhaustive.

- annual financial statements, quarterly results and interim financial statements, cf. Section 2.3;
- Shareholders' meetings shall be open to the public and changes to Articles of Association must be published, cf. Section 2.4.
- Elections of Directors, cf. Section 5.1 above;
- A declaration as to whether the company complies with the Guidelines on Corporate Governance and, if not, why, cf. Section 2.5.9;



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