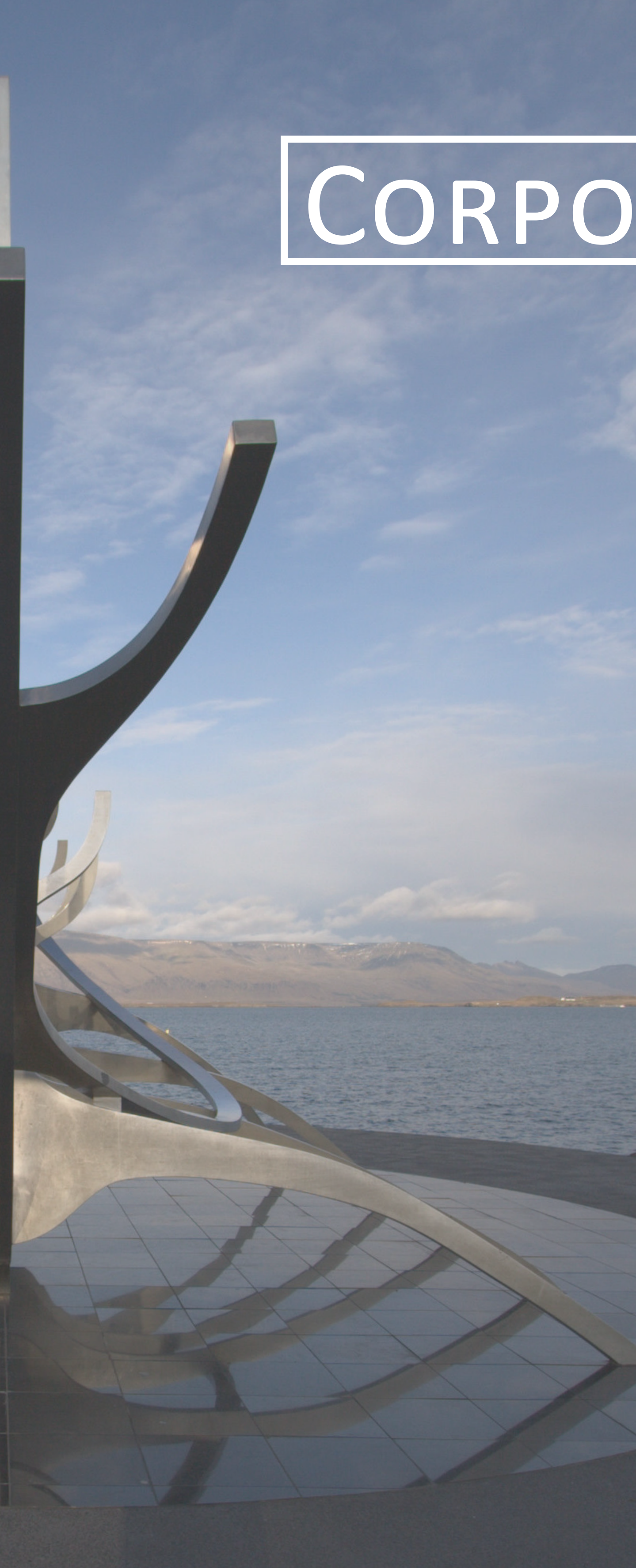

# CORPORATE

## GOVERNANCE

GUIDELINES

3. EDITION

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# CORPORATE GOVERNANCE

## GUIDELINES

JUNE 2009

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# Foreword

The setbacks suffered over recent months have raised many questions concerning the infrastructure of Iceland's business sector, its focus and responsibilities. There have been calls for a revised approach involving a new set of values. This demand is both reasonable and necessary. Distrust towards companies and the business sector bears witness to many things that might have been better done differently, and it is evident that action must be taken to reclaim lost goodwill and to build up credibility in the business sector. Such action is a basic precondition for the growth of a dynamic and healthy business sector.

The Icelandic business sector needs to establish for itself certain values as a foundation for its existence and its decisions. In this respect, one must look to the past and learn from mistakes as well as successes. As regards the former, experience teaches that narrow short-term interests cannot and must not be the foundation for the Icelandic business sector in the future. Therefore, a new set of values entails increased stress on transparency and improved access to information. In addition, business decisions must be based on sustainability with a goal of future prosperity for individuals and society as a whole.

In the same manner, it is important to look at the positive aspects of the work of recent years. The operation of a large number of businesses has been exemplary. These have created valuable knowledge which will be of invaluable assistance in the future. It is particularly important that the entrepreneurial spirit and daring that has long characterised the Icelandic business sector is not lost. Although at present every effort is being directed to rebuilding on new foundations, the dynamism and entrepreneurial spirit of individuals will be a prerequisite for progress in the foreseeable future.

The business sector will need to take action. Icelandic companies should lead the way by setting a good example and should show, through action, their intention to correct what has gone wrong. This means that companies and managers must adopt good methods of governance and should expect the same from others. This lays the foundations for reclaiming confidence and credibility in the business sector and is to the benefit of society as a whole, and to companies and managers. Systematic and determined compliance with these Guidelines, both in word and spirit, is the first step in this journey.

# Introduction

In 2004, the Iceland Chamber of Commerce, the Confederation of Icelandic Employers and NASDAQ OMX Iceland published the first Guidelines on corporate governance in Iceland. The Guidelines were intended to guide companies on how to arrange relations between shareholders, boards and management. The Guidelines were prepared in accordance with international points of focus in this field at a time when discussions on corporate governance were prominent. The Guidelines were revised a year later and have remained unaltered ever since.

The Guidelines involved an initiative on the part of the business sector to adopt stricter working procedures than required by law in order to strengthen corporate infrastructure and to increase the public's confidence in the sector. They included increased company responsibility towards shareholders, clients and society as a whole and were a means to strengthen the company in question, which in turn is the prerequisite for increased competitiveness in the Icelandic business sector and, at the same time, better living standards. This position is no less important today.

The reception to the Guidelines caused some disappointment. Unfortunately, it could be said that the current disastrous period suggests that there are faults in the governance of many companies, both in Iceland and abroad. The international financial crisis has forced further discussion on the involvement of governance in the present situation and has resulted in the identification of various shortcomings in this field. In light of the fact that the Icelandic business sector has been particularly damaged, it is appropriate that the response here be firm and effective, with the aim of permanently mending governance in the Icelandic business sector.

The first step on this journey is a revision of the earlier Guidelines on governance. In this edition, particular account was taken of similar guidelines from other countries and of the recommendations of the European Commission and the Organisation for Economic Co-operation and Development (OECD). The Guidelines, now considerably amended, include both additional and more detailed provisions than the earlier Guidelines and contain increased requirements for corporate management in nearly all fields.

The main additions and changes involve requirements for the independence of Directors, communications and goal setting, the role of the Chairman of the Board, internal controls and risk management, remuneration policy, as well as focusing on the disclosure of more detailed information. This new edition also discusses the code of ethics and corporate social responsibility, which is known to substantially affect the reputation of corporations and their success in the long term. This type of emphasis would give the Icelandic business sector an opportunity to gain an edge internationally and is in line with goals for sustainable development and the development of resources, something that has long been of great interest to Icelanders.

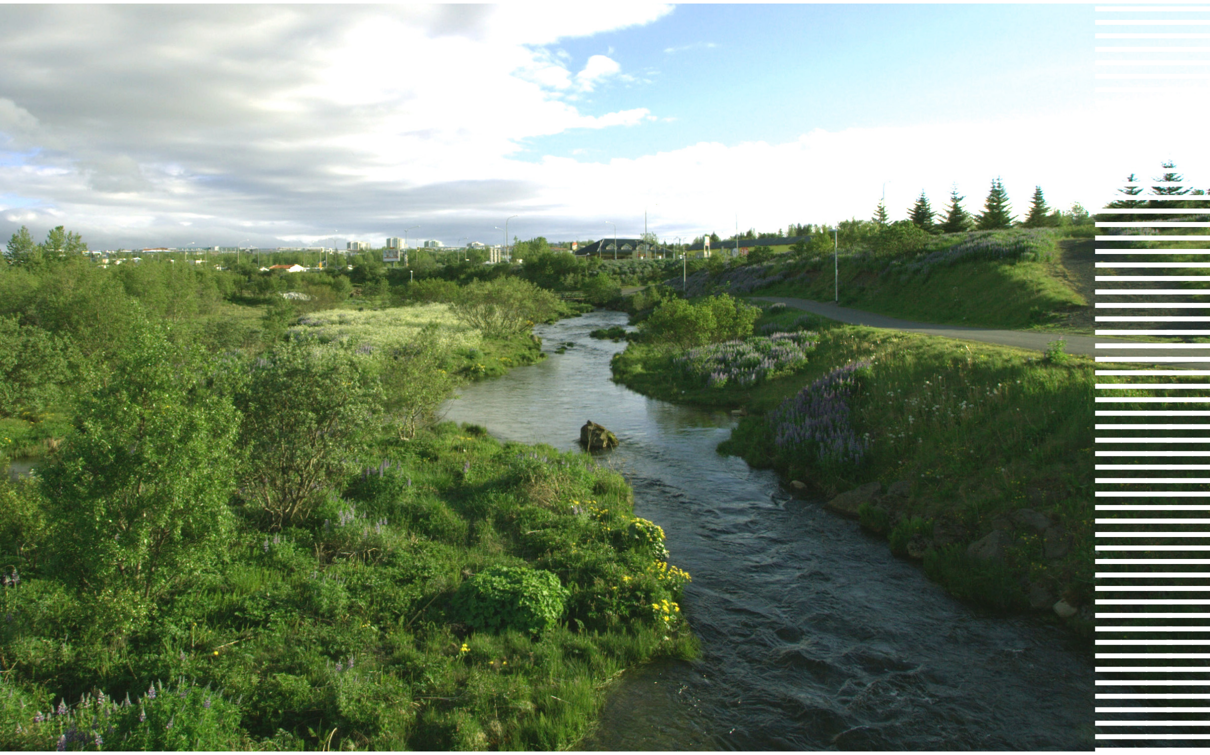
These Guidelines are suitable for and are particularly directed at undertakings that are considered public-interest entities[1], whether listed on a stock exchange or not. They are also suitable for other public limited companies and private limited companies and may in whole or in part be useful for other undertakings or institutions given that they contain guidelines on the work and job responsibilities of nearly all managers, regardless of the size and type of undertaking. In addition, the Guidelines apply to companies owned by the state and local authorities. The publication *"Corporate Governance of Publicly Owned Enterprises"*, issued in November 2008, contains further provisions on special stipulations for such undertakings. Although the goal of the Guidelines is to strengthen and promote firms, strict compliance is not mandatory. Listed firms, however, are required to comply with these Guidelines, as is indicated in the NASDAQ OMX rules for the issuers of financial instruments. As before, the basic requirement is that companies follow the rule of "comply or explain", which states that if a company does not comply with the Guidelines in all matters, it must then disclose any non-compliance and provide the reason for it in the annual accounts or in the annual report.

Members of the working group on corporate governance were: Thordur Fridjonsson, CEO of NASDAQ OMX Iceland (Chairman); Finnur Oddsson, Managing Director of the Iceland Chamber of Commerce; Gudrun Bjork Bjarnadottir, Attorney at the Confederation of Icelandic Employers; Hildur Arnadottir, Auditor at Bakkavor Group; Thor Sigfusson, Chairman of the Confederation of Icelandic Employers; Thoranna Jonsdottir, Director of Communications Business Development at Audur Capital; Thordur Magnusson, Chairman of the Board of Eyrir Invest. The Project Manager was Haraldur I. Birgisson, General Counsel of the Iceland Chamber of Commerce. The working group wishes to express their thanks for the assistance and co-operation of the Business Advisory Services of PricewaterhouseCoopers hf.; the Ethikos Centre for Corporate Social Responsibility at Reykjavik University; the Institute for Ethical Research at the University of Iceland; Thorkell Sigurlaugsson, Executive Director of Development at Reykjavik University; and David Scheving Thorsteinsson.

[1] Under Act No. 79/2008 on Auditors, cf. Act No. 80/2008 on Annual Accounts, the following undertakings are considered public-interest entities: a) Legal persons having a registered domicile in Iceland and having their securities listed on a regulated securities market in a state within the European Economic Area, in a member state of the European Free Trade Association or in the Faeroe Islands; b) Pension funds with a fully valid operating permit; c) Lending institutions pursuant to the Act on financial undertakings; d) Undertakings that have a licence to operate insurance operations in accordance with the Insurance Act.

The Chamber of Commerce, the Confederation of Employers and NASDAQ OMX Iceland plan to review these Guidelines on a regular basis taking into account rapid developments in this field, both in Iceland and overseas. Mention may be made here of the Ethikos Action Plan on Social Responsibility, the results of the Althingi Special Investigation Committee Ethics Team, the Walker Report of the British authorities and the review of the British Code on Good Corporate Governance.

The adoption of guidelines on good governance is one of many important steps toward rebuilding the Icelandic business and economic sector. In order to increase the likelihood of success, extensive co-operation with companies, investors, media, educational institutions and research entities on compliance with the Guidelines is called for. Those responsible for the publication of these Guidelines will place great importance on compliance with the Guidelines, as the interests of the Icelandic business sector and society as a whole are too great to allow substantial non-compliance.



# 1. Shareholders´Meeting

Shareholders hold the decision making powers in the affairs of the company at shareholders meetings[1]. Shareholders' meetings are the supreme authority in the company's affairs. The meetings must be organised so as to permit shareholders to exercise their ownership rights in an effective and informed manner.

## 1.1 Information on the Annual General Meeting

When the time and date for the annual general meeting (AGM) has been decided, preferably no later than two months before the end of the company's accounting year, it is recommended that the date is posted on the company's website together with the deadline for shareholders to submit motions and/or proposals to be discussed at the meeting.

It is proposed that the language to be used at the meeting be specified in the convening notice as well as the language of the documents for the meeting. If the meeting is conducted in, or if the documents are in, a language other than Icelandic, it is recommended that the main points of the agenda are also available in a summary in Icelandic. In addition, it is recommended that the notice specify if a translation of the introductory talks and documents will be made available to the shareholders.

## 1.2 Attendance by Management

The Chairman of the Board and the required majority of the Directors[2] must be present at shareholders' meetings, as must the Chief Executive Officer (CEO). In addition, the presence of the company's auditor and no fewer than one committee member from all the Board's sub-committees is recommended at shareholders' meetings if appropriate.

The Board shall post the following information on candidates to the Board on the company's website as early as possible, and no later than two working days before the AGM.[3]

- Name, date of birth and address.
- Education, chief occupation and professional experience.
- Date of first election to the company's Board.
- Other commissions of trust, e.g. membership on boards of other companies.
- Shares in the company, whether direct ownership or through associated parties.
- Option agreements with the company.
- Interest links to the company's main clients and competitors and large shareholders in the company.[4]

If there is a Nomination Committee in the company, the Committee's proposals for the composition of the Board must be ready at least five working days prior to the company's AGM.[5]

A nominated party or one who runs for office as a Directors must be present at the company's AGM unless there is a valid reason for his absence. If circumstances prevent the management from attending a shareholders' meeting in the company, it is recommended that their participation is ensured by other means e.g. by electronic means.

## 1.3 Election of the Chair of the Meeting

If the company has a Nomination Committee, the Committee shall propose a Chairman to chair shareholders' meetings in the company. The Committee's proposal must be stated in the convening notice.

If there is not a Nomination Committee in the company, the meeting elects a Chairman for the meeting from among the shareholders or others unless the company's articles of association provide otherwise.[6]

## 1.4 Minutes of Shareholders´Meetings

The meetings secretary and Chairman must validate the minutes of the shareholders' meeting if so authorised by the meeting.[7]

Minutes of earlier shareholders' meetings are to be accessible on the company's website. A list of those shareholders and shareholders' representatives who have attended the meetings need not be posted on the company's website.

## 1.5 Share Registry

The Board must ensure that the share registry contains correct information at all times. Information on shareholders' voting rights must be entered into the registry. The registry must also state any associations the company has with corporate groups.

Copies of the company's share registry must be available to shareholders at the shareholders' meeting. The registry should preferably also indicate the names of the representative of the companies that are registered shareholders in the company for which the shareholder meeting is held.

[1] Here and elsewhere in the Guidelines, the reference is both to the AGM and other shareholders' meetings, unless specifically mentioned that reference is only made to the AGM.
[2] Refers to the number needed for a quorum of the Board. The Board has a quorum when a majority of the Board convenes for a meeting unless the company's articles of association provide otherwise.
[3] Cf. paragraph 1 of Article 63 (a) of the Act on Public Limited Companies No. 2/1995 (hereinafter referred to as the PUBLC Act.).
[4] A significant shareholder is anyone who controls at least 10% of the total share capital or weight of votes in the company, alone or in co-operation with associated parties.
[5] Cf. guideline C.3.
[6] Cf. paragraph 1 of Article 90 of the PUBLC Act.
[7] Cf. paragraph 5 of Article 90 of the PUBLC Act.

# 2. The Board

## 2.1 Main Role and Duties

The Board of Directors bears principal responsibility for the operation of the company in which it carries out the supreme authority between shareholders' meetings.

The main role of the Board is as follows:

- To promote the company's development and success in the long term and to supervise its overall operations and the executive directors of the company.
- To ensure that the interests of all shareholders are guarded at all times, as Directors of the Board are not to act specifically in the interests of the parties who gave them support in their election to the Board.
  - The Board must treat all shareholders who hold the same class of shares in the same manner.
  - When the decisions of the Board can have a different affect on different classes of shares, the Board must seek to ensure equal treatment.
- To take the initiative, together with the CEO[1], in formulating policies and setting goals and risk parameters for the company, both for the shorter and longer term.
  - The company's goal setting should at least cover its activities, financial information, its social role and compliance with laws and regulations.
  - The Board must ensure that, in its decisions, a wide range of interests are taken into consideration, such as employees, suppliers and society in general, which can have an affect on the long-term performance of the company.
- To be ultimately responsible for the company's activities and operations. In order to carry its responsibilities, the Board needs to have an overview over the operations and to exercise reasonable restraint on the company's executive directors.
  - The Board must ensure a clear definition and allocation of responsibilities with respect to operations, the implementation of policies and the objectives of the company within all its departments.
  - The Board must assess the performance of the company's executive directors and the manner in which its policy formulation is implemented.
  - The Board must supervise and assess the effectiveness of the Board's sub-committees.

- To administer the recruitment and dismissal of the company's CEO.
- To establish written rules on working procedures for itself and regularly assess its own work.

It is important that the Board determines the proper processes for its main duties, in particular in connection with internal controls in order to increase transparency in the operation of the company and to ensure efficiency in its work.

The Board must meet sufficiently frequently to enable it to perform its responsibilities efficiently. The number of Board meetings and committee meetings and their attendance must be stated in the company's corporate governance statement (see section 6).[2]

## 2.2 Size and Composition of the Board

The Board must be of a size and composition that makes it possible for the Board to discharge its duties efficiently and with integrity.

The composition of the Board must take into account the operation and policies of the company, its development stage and other relevant factors in its operation and environment. Directors must be diverse and have a wide range of capabilities, experience and knowledge.

In light of the monitoring role of the Board, setting further limits to the number of executive managers on the Board than required by law is reccommended[3]. This means that, as a rule, only one Director should be from among day-to-day managers in the company or its subsidiaries.

## 2.3 Co-operation and Goal Setting

The Board must seek to engage in regular discussions on the manner in which it intends to discharge its duties, the areas which it will focus on, what communications and procedural rules will be upheld and what the main goals of the Board are.

Board activities have proved to be most successful when characterised by open discussion and constructive criticism. One of the key factors in the work of the Board is that its Directors pose demanding questions of a nature to encourage the close examination of issues and informed decision making.

It is particularly important to attend to the above aspects when a new Board convenes or when new Directors join the Board.

## 2.4 Independent Directors

The majority of Directors must be independent of the company and its day-to-day managers. At least two Directors[4], moreover, must be independent of the company's significant shareholders.

One of the most important duties of the Directors is to monitor those who are responsible for the company´s day-to-day operation. This is why it is recommended that the majority of the Board consist of Directors who are independent of the company and that, of these, at least two Directors are independent of significant shareholders in the company.[5]

The participation of independent Directors, moreover, is for the purpose of limiting the influence of significant shareholders on the company's Board and thereby further ensuring that the Board focuses on protecting the company's overall interests rather than protecting the interests of particular shareholders.

## 2.5 Evaluation of Independence

The Board itself evaluates whether Directors are independent of the company and its significant shareholders, unless the Nomination Committee has been entrusted with this task. The Board, moreover, evaluates the independence of new Directors before the company´s AGM and make the result of such evaluation available to shareholders.

A Director is not independent of the company:

1. If he/she is or has been an employee of the company or group during the three years prior to the commencement of Board membership.
2. If he/she receives or has received payments from the company, or its day-to-day managers, apart from a director's fee, e.g. as a consultant or contractor, during the three years prior to commencement of Board membership.
3. If he/she has close family ties with any of the company's advisers, Directors or executive managers.
4. If he/she is one of the executive manager in another company which is or has been engaged in considerable business relations with the company as e.g. a client, supplier or partner.
5. If he/she is one of the executive manager of another company where one of the executive managers is a Director of the Board of the company.
6. If he/she is engaged in considerable business relations with the company or has considerable business interests in the company.
7. If he/she is, or has been during the three years prior to becoming a Director of the Board, the company´s auditor, examiner or a co-owner or an employee of the company's present auditor or auditing firm.
8. If he/she is party to a performance-linked remuneration system in the company.
9. If the Board is aware of any other issues where the interests of the Director and the company significantly overlap.

A Director is not independent of the company's significant shareholders:

1. If he/she has direct or indirect control of the company or is in such a relationship, cf. items 1 and 2 above, with a party who has control of the company.
2. If he/she owns a significant share in the company, or is in such a relationship, cf. items 1 and 2 above, with a party who owns a significant share in the company.[6]
3. If the Board is aware of any other issues where the interests of the Director and significant shareholders substantially overlap.

When the Board evaluates the independence of a Director, it must specifically examine:

1. Whether he/she is a participant in the same performance- and/or share-related remuneration system as other employees in the company which could entail substantial financial interests for him.
2. Whether he/she has been an independent Director in the company for more than seven consecutive years.
3. Whether individuals or legal persons connected to him are in such a relationship with the company as described above.
4. Whether there are any other factors and/or circumstances that can have an effect on the independence of the Director, both in actuality and appearance.

If the majority of the Board is not independent of the company or its significant shareholders, this must be stated in the company's governance statement, together with the appropriate explanations.

Diversity and breadth in the capabilities, experience and knowledge of Directors is one of the prerequisites enabling the company's Board to discharge its duties efficiently and with integrity and to ensure that the Board can apply neutral and independent judgment in its duties. The above criteria for independence should not be interpreted in such as manner as to prevent such diversity and breadth. In the event that a particular Director does not meet the above conditions but is nevertheless considered extremely competent for the work due to experience, education or other reason, the governance statement must explain the manner in which the Board intends to prevent conflicts of interest that could arise in his work as a Director of the Board.

## 2.6 Personal Information on Directors

Directors must provide personal information to facilitate the above evaluation for the Board, or the Nomination Committee, and must notify of any changes to their circumstances which could affect whether they can be considered independent.

The following information on Directors must be included in the governance statement:

- Name, date of birth and address.
- Education, chief occupation and professional experience.
- Date of first election to the Board.
- Other commissions of trust, e.g. membership on boards of other companies.
- Shares in the company, whether direct ownership or through associated parties.
- Option agreements with the company.
- Connections with principal clients and competitors of the company and large shareholders in the company.

## 2.7 Internal Controls and Risk Management

The Board is responsible for establishing an active system of internal controls. This means, among other things, that the arrangement of the internal controls system must be formal and documented and its functionality must be verified regularly.

An active internal controls system formalises the manner in which the company works towards its goals, distributes responsibility in its internal activities and explains the responsibility of the Board in such work. An active internal controls system, therefore, will determine how the Board performs its monitoring role in the operation of the company and its daily management. It is important the internal controls system follow the formal framework in order to make it easier for the Board to assess its effectiveness at any particular time.

The Board is at all times responsible for the organisation and functionality of the internal controls system. The Board may assign the implementation of certain aspects of the internal controls to parties within the company. However, it should be done in such a manner that the Board is informed of the parties' actions and how they limit risks. When responsibility for the implementation of control activities is assigned to particular sub-units or managers within the company, this should be done formally so that there is no uncertainty with respect to where the responsibility lies and how to respond to deviations.

The purpose of internal controls should be to provide reasonable certainty that the company can attain its goals with respect to the following factors:

- Success and efficiency in operations.
- Providing dependable and rightful financial information to external parties.
- Complying with laws and regulations that apply to the business.

Internal controls are generally divided into five main parts:

- **Monitoring environment:** This entails the management's view that internal controls are important in ensuring effectiveness and responding to the risk of substantial loss or damage caused by fraudulent behaviour or mistakes.
- **Risk assessment:** An assessment is made of substantial risk factors which may prevent the attainment of success and efficiency goals, reliable financial information and compliance with laws and regulations.
- **Supervisory activities:** All the actions incorporated into daily operations to respond to risk, such as the separation of jobs, suitable rules of procedure and work processes.
- **Information and communication:** This factor covers IT systems and any kind of communication that supports internal controls.
- **Management control:** This includes controls and follow-ups by management, making sure that the internal controls are satisfactory at any particular time. The Board, however, may assign an Audit Committee this role and/or commission an internal audit department to monitor the arrangement and effectiveness of the internal controls.

It is important that the company's internal controls and risk management is given sufficient attention by the Board. To ensure that this is the case, it is preferred that the Board regularly holds special Board meetings for the sole purpose of reviewing issues relating to internal controls. The Board should request the presence of the internal and external auditors together with the CEO and Audit Committee at such meetings.

Active internal controls mean that the Board applies systematic risk management to analyse what risk factors could prevent the company from achieving set goals and that remedial action is taken to minimise the anticipated effects of such risk factors. To this end, the Board should assess, on a regular basis, the company's finance, liquidity and equity and perform stress tests if appropriate. In addition, the Board should adopt processes that encourage the use of risk assessment to analyse what events could prevent the company from achieving its goals and reduce the risk of such events.

The Board should, in consultation with the Audit Committee, regularly perform evaluations of the company's internal controls and risk management and take action to remedy any defects, if necessary.

The main aspects of the company's internal controls and risk management must be described in its governance statement.

## 2.8 Rules on Working Procedures

The Board shall establish its own written rules of procedure that further address the role and execution of the work of the Board.[7]

The rules of procedures should deal with the allocation of tasks among Directors and the relations between the Board, the Chairman of the Board and the CEO. Such information makes it easier for shareholders to assess the work of the Board.

The Board's rules of procedure should cover the following items:

- Allocation of tasks among Directors.
- The job descriptions for the Board, the Chairman of the Board and the CEO.
- The convening of Board meetings, their frequency, participants and the arrangement of meetings.
- Decision making powers and voting among Directors.
- Documents for meetings and minutes.
- Board sub-committees, their duties and decision making powers.
- Procedures for annual performance assessments.
- Gathering and disclosing to the Board information from the CEO and sub-committees.
- Professional secrecy and confidentiality.
- Ineligibility.
- Links to other rules within the company, such as guidelines on good governance and other rules as applicable e.g. from the Financial Supervisory Authority and the NASDAQ OMX.

It is preferred that the Boards rules on working procedure are revised at least annually.

## 2.9 Performance Assessment

The Board must annually evaluate its work, size, composition and practices, and must also evaluate the performance of the CEO and others responsible for the day-to-day management of the company and its development.

The annual performance assessment is intended to improve working methods and increase the efficiency of the Board. The assessment entails e.g. evaluation of the strengths and weaknesses of the Board's work and practices and takes into consideration the work components which the Board believes may be improved. This evaluation may be built upon self-assessment, although at the same time, the assistance of outside parties may be sought as appropriate. The Board should preferably also evaluate the work of its sub-committees.

The evaluation must, among other things, include an examination of the general work procedures employed by the Board or particular sub-committees. At the same time, an examination must be made as to whether important matters relating to the company have been sufficiently prepared and discussed within the Board. Furthermore, the input of individual Directors must be considered with respect to both attendance and participation in meetings. The Board must respond to the results of the assessment by acknowledging its strengths and weaknesses. This could e.g. entail that other Directors of the Board assume the seats of the present Director or that particular Directors decide not to stand for re-election.

The Board must assess the performance of the CEO and day-to-day managers at least annually. In such cases, no Director of the Board who is at the same time one of the company´s managers may be present during such assessment. The Chairman of the Board must present the result of the assessment to the company's CEO and managers and discuss with the relevant person the manner in which to address weaknesses and/or improve the use of strengths.

Board Directors should meet without the Chairman of the Board present at least annually in order to evaluate his performance.

## 2.10 Ethics and Social Responsibility

It is preferred that the Board establishes a set of written rules for the Board, the management and the employees, providing for the company's code of ethics and social responsibility.

The Board should, in consultation with the employees and other stakeholders, determine the values on which the company's operation is based. In order to make it easier for the company's employees and management to adhere to the values, the Board should prepare a written code of ethics and formulate its policy on social responsibility.

By measures of this kind, the company will not only promote a healthier economy and improved relations with stakeholders, but also reinforce its operating basis with an increased appearance of reliability and credibility, an improved sense of risk, happier employees and, in the end, improved competitiveness.

The Board is responsible for establishing these rules, which should take account of the company's operations and operating environment.

It is preferred that the rules involve an approach of the following points:

- **Company values:** The Board should determine and set the values upon which the company's business is based, both subjective (such as honesty, mutual respect, equality and fairness) as well as objective (such as profitability, product quality, wholesome working environment, happy and effective employees).

- **Social responsibility:** The company should formulate a policy on social responsibility and relations with stakeholders and should formulate ways to ensure follow-ups of such policy. To this end, the policy must recognise and comply with applicable laws and regulations, human rights, social factors, employees' entitlements, environmental and climate issues and entail an uncompromising position against corruption in the company's activities.

- **Conflicts of interest:** The company should establish for itself a policy that would effectively prevent conflicts of interest arising between the company and its employees, Directors and their spouses.

- **Agency problem:** The company should systematically counter the opportunity of employees and Directors to abuse their powers to the detriment of the company and others, e.g. by the use of insider information or other confidential information.

- **Confidentiality:** The company's employees should maintain confidentiality with respect to information relating to the company and its clients unless otherwise legally required.

- **Compliance with the law:** The company should actively encourage compliance with laws and regulations, both their wording and purpose, and various guidelines and recommendations from public authorities that apply to its operations.

- **Disclosure of information on failures:** The company should encourage good ethics and, at the same time, encourage employees to consult with their superiors, the company's management or other pertinent parties within the company in the event of ethical uncertainties in actions or decisions within the company. In addition, the company should ensure that such notifications, given in good faith, are not met with sanctions of any kind.

## 2.11 Shareholders´ Relations

The Board's relations with shareholders shall be characterised by honesty and be unambiguous and co-ordinated.

An effective and accessible arrangement for the communications between shareholders and the Board should preferably be established. Shareholders should thereby have the opportunity to explain their views on the company's operation to the Board and to ask the Board questions.

The Board should be notified of all proposals or questions from shareholders and should supervise of the company's response.

[1] In this discussion and elsewhere in the Guidelines, references to the CEO are references to the manager who is hired by the Board, not the managers of departments or divisions.
[2] A statement of corporate governance must be published in a separate section of the company's annual accounts.
[3] Paragraph 2 of Article 65 of the PUBLC Act provides for a prohibition against the majority of the Board consisting of persons who are at the same time the CEO´s of the company.
[4] This refers to a Board consisting of five members.
[5] A significant shareholder is anyone who controls at least 10% of the total share capital or weight of votes in the company, alone or in co-operation with associated parties.
[6] A substantial shareholding means shares representing at least 10% of the company's share capital, its cash funds or particular classes of shares in the company, irrespective of whether the share is owned by a Director of the Board or other parties associated with him.
[7] Cf. paragraph 5 of Article 70 of the PUBLC Act.

# 3. Directors of the Board

## 3.1 Chairman of the Board

The Chairman of the Board bears the responsibility of the Board fulfilling its role in an effective and organised manner.

The Chairman of the Board carries the main responsibility for the activities of the Board and ensuring that the Board works under the best possible working conditions. The Chairman of the Board has the obligation to keep all Directors informed of issues concerning the company and must encourage the activity of the Board in all decision making. It is important that a job description is available for the work and responsibilities of the Chairman of the Board as well as a description of the manner in which he/she is expected to perform his responsibilities.

Such job description should preferably contain provisions stipulating that the Chairman of the Board:

- Ensures that new Directors of the Board receive necessary information and guidance in the procedures of the Board and the company's affairs, including the company's policies, its objectives, risk parameters and operations.
- Ensures that the Board updates regularly its knowledge of the company and its operations, in addition to ensuring that the Board receive, generally in its work, detailed and explicit information and data in order to be able to perform its work.
- Seeks to arrange for Directors proper guidance regarding the main issues involving corporate governance e.g. regarding their statutory duties and responsibilities or ensuring that Directors attend courses of that sort.
- Bears the responsibility for relations between the Board and shareholders and informs the Board of the shareholders' point of view. The Chairman of the Board, moreover, should encourage open communication within the Board and between the Board and the company's management.
- Takes the initiative in the preparation and revision of the Board's rules of procedure.
- Organises the agenda for the meetings of the Board in partnership with the company's CEO, supervise their convening and chairing. The Chairman of the Board should ensure that Board meetings allow ample time for discussions and decision making, in particular with respect to larger and more complicated issues.
- Follows progress in the execution of Board decisions within the company and confirms their implementation to the Board.
- Ensures that Board Directors make an annual assessment of their work and that of the sub-committees.

The Chairman of the Board must not assume responsibilities for the company other than those that are considered a normal part of his work as a Chairman, with the exception of individual projects which the Board assigns to him to perform.

## 3.2 Directors

Anyone who is elected as Director must possess the necessary qualification to be able to fulfil its duties as Directors and be able to devote the time required by such duties. Independent exercise of judgment is a precondition for all decision making, whether or not Directors are considered independent.[1]

Effective Board membership requires an understanding of the company's activities. An essential requirement for the Board to deliver good work and good performance is that it consists of individuals who complement each other with different knowledge, abilities and skills. Each Director must have sufficient time to devote to its duties in the company´s service.

Board Directors must:

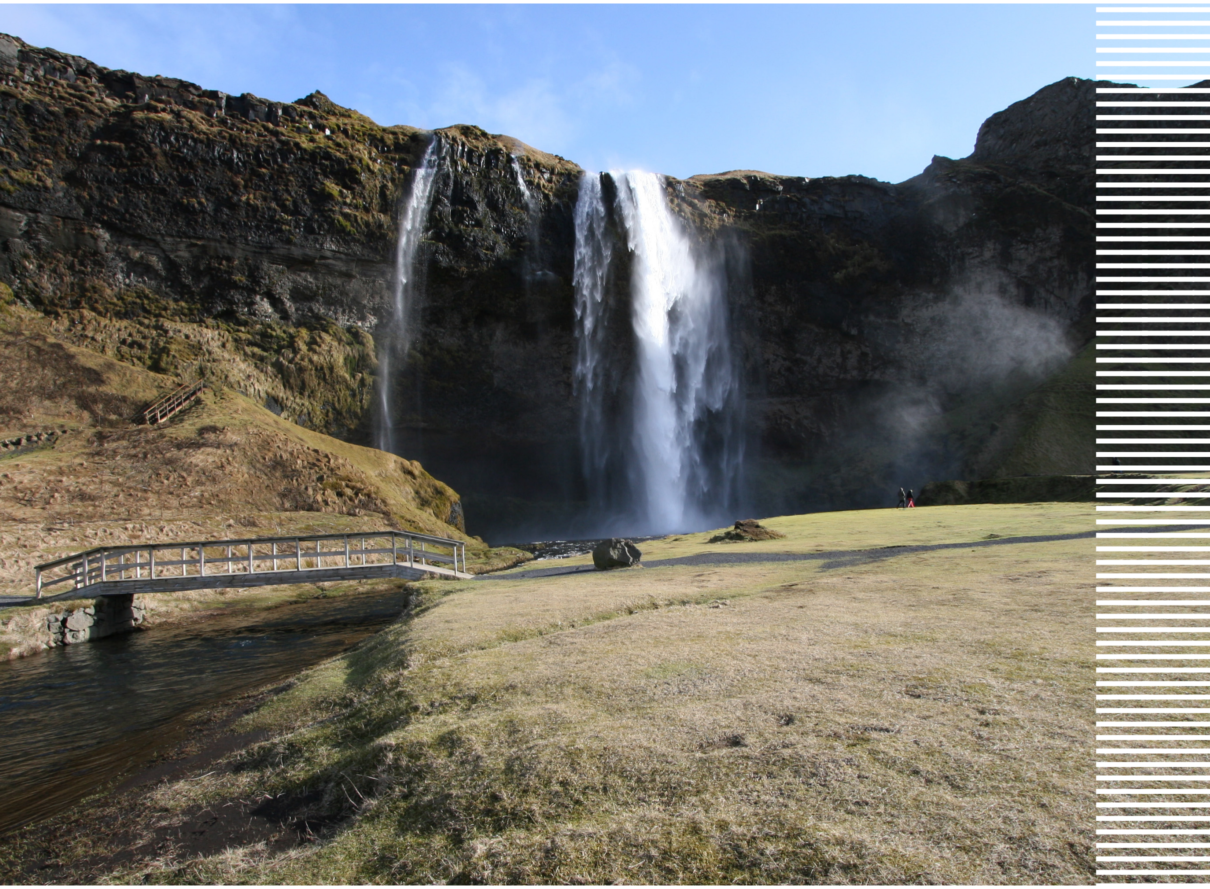
- Make independent decisions in each individual instance.
- Understand the role of the Board, their own role and responsibilities, as well as have knowledge of the laws and regulations that apply to the running of a business and the activities of the company.
- Understand the objectives and projects of the company and have an understanding of how they should organise their Board membership responsibilities in order to contribute to the achievement of these objectives.
- Call for and study all documents and data that they feel that they need in order to have a full understanding of the operations of the company and to be able to make informed decisions.
- Ensure that internal controls are in place and that the decisions of the Board are complied with.
- Verify that the laws, rules and regulations are adhered to at all times.
- Encourage a good atmosphere within the Board.
- Prevent their affairs, whether personal or business related, from leading to a direct or indirect conflict of interest between themselves and the company.

Directors should have access to independent expert advice at the company's expense, if they feel that would be necessary in order to be able to reach independent and informed decisions.

A Director must ensure that his views in connection with individual issues are entered in the minutes if he/she is not content with the decision making of the majority of the Board. In the event that a dispute is the cause of the resignation of a Director, he/she must indicate this in a written statement to the Board.

If the decisions of the Board pertain to the affairs of individual Directors, e.g. negotiations between the company and such a Director, such decisions should be taken by independent Directors of the company[2]. In addition, the Director in question should leave the meeting while the Board addresses such issues. A Director must disclose such issues of this type as soon as they arise as well as if he/she becomes aware that he/she cannot be considered an independent Director.

[1] This guideline applies alike to the Chairman of the Board as well as to all other Directors.
[2] Cf. paragraph 1 of Article 72 of the PUBLC Act.



# 4. The Chief Executive Officer

The CEO is responsible for the day-to-day operation of the company and must, in this respect, follow the policies and instructions laid down by the Board[1]. The CEO must at all times conduct his work with integrity and take account of the company´s interests.

The CEO must provide information on himself to ensure that shareholders are informed of main points relating to him. The following information on the CEO must be published in the company's corporate governance statement:

- Name, date of birth and address.
- Education, chief occupation and professional experience.
- Date of appointment.
- Other commissions of trust, e.g. membership on Boards of other companies.
- Shares in the company, whether direct ownership or through associated parties.
- Option agreements with the company.
- Connections with principal clients and competitors of the company and significant shareholders in the company.

The CEO must ensure that Board Directors are regularly provided with accurate information on the company's finances, development and operation to enable them to perform their duties.

The information needs to be in the form and of the quality determined by the Board. Information and data should be available to Directors of the Board in good time for Board meetings, and between such meetings. All Directors must receive the same information. Moreover, information must be available when needed and as up-to-date and accurate as possible. The should preferably determine the general rules applicable to information provision by the CEO in its operating rules.

The CEO must submit any other projects undertaken by him, which are unrelated to the company, to the Board for discussion.

[1] Cf. paragraph 1 of Article 68 of the PUBLC Act.

# 5. Sub-committees of the Board

Proper organisation of the work of the Board is a prerequisite for the smooth operation of the company and the management's work. The establishment of sub-committees can improve procedures in the issues that the Board is obliged to attend to and can make its work more effective. The Directors of the Board involved in such specialised committees can focus better on the tasks entrusted to them than they would when the entire Board is assembled. It is important that the sub-committees regularly inform the Board of the main results of their work. Sub-committees operate under the authority of the Board and must submit to the Board a report on their activities at least once a year. The Board is responsible for the appointment and activities of the sub-committees.

Sub-committees must establish clear written rules of procedure for themselves. The rules are to be posted on the company's website to make it easier for them and others to understand their roles and responsibilities. The rules of procedure shall state that new committee members receive instruction and information on the work and procedures of the committee. Committees, moreover, must ensure good communications with the company's management.

Board sub-committees must ensure that Board Directors are regularly provided with accurate information on the committees' principal work. The information needs to be in the form and of the quality determined by the Board. Information and data is to be available to Directors of the Board in good time for Board meetings, and between such meetings. All Directors must receive the same information. Moreover, information must be available when needed and as up-to-date and accurate as possible. The Board should preferably determine the general rules applicable to information provision by the committees in its operating rules.

## 5.1 Establishment of Sub-committees

The Board assesses the need for establishing sub-committees according to the size and scope of the company, and the composition of the Board. The company's corporate governance statement must state the establishment and appointment of committees.

It may be important that particular tasks assigned to the Board receive further discussion and analysis in smaller groups. It is therefore considered appropriate to appoint Board sub-committees to address certain aspects, particularly those that relate to financial supervision, remuneration to the CEO and remuneration systems for day-to-day managers.

The role and principal tasks of sub-committees must be stated in their rules of procedure. In this respect, it is also possible to refer to these guidelines in the rules of procedure.

## A.1 Audit Committee

Public-interest entities must[1] appoint an Audit Committee. Moreover, the appointment of an Audit Committee is recommended if the scope of the company is such that it is considered important that surveillance and reporting on financial affairs receive further discussion and analysis in small groups rather than by the entire Board.

The Audit Committee is responsible for reviewing financial information and the arrangement of information provision from managers. The Committee must verify that the information provided to the Board as relates to the operation, standing and future prospects of the company is as reliable and provides as clear a view of the company's position as current from time to time as possible. The Audit Committee must submit a report on its activities to the Board on an annual basis at least.

The Audit Committee must establish written rules of procedure for itself. These rules should preferably stipulate, among other things, that the Committee assess its work and the work of individual Committee members.

On the execution of its work, it is important that the Audit Committee has extensive access to data from managers and internal and external auditors. The Committee may request reports and commentaries from such parties as relates to the Committee's work.

Companies, other than public-interest entities, that have not already established an Audit Committee, must consider annually whether the establishment of such a Committee is necessary.

## A.2 Appointment of Committee Members

The Audit Committee must consist of at least three members, the majority of whom must be independent of the company and its day-to-day management[2]. Committee members must have the qualifications and experience necessary for the work of the Committee.

The Audit Committee must be established no later than one month after the AGM. The Board is responsible for the establishment of the Committee.

Committee members must be independent of the company's auditor/auditors and its day-to-day managers. The Committee majority must, moreover, be independent of the company, and at least one member of the Committee must be independent of significant shareholders. The CEO and other day-to-day managers may not be members of the Committee.

Committee members must have qualifications and experience in accordance with the activities of the Committee, and at least one member must have sufficient expertise in the field of accounting or auditing. On assessing whether the Committee member has such knowledge, the following criteria may be used:

1. Knowledge of generally accepted accounting principles.
2. Experience in the preparation and analysis of financial statements or auditing.
3. Knowledge of internal controls relating to the preparation of financial statements.

## A.3 Role of the Audit Committee

The Audit Committee must seek to ensure the quality of the company's annual accounts and other financial information and the independence of its auditors.

The role and principle tasks of the Committee must be stated in its rules of procedure. The Audit Committee must, among other things, have the following role[3] irrespective of the responsibility of the Board, manager or others in this field:

1. Monitor working processes in the preparation of financial statements.
2. Monitor the organisation and effectiveness of the company's internal controls, internal auditing, if applicable, and risk management and other supervisory activities.
3. Monitor the auditing of the company's annual accounts and consolidated accounts.
4. Assess the independence of the auditor or auditing firm and monitor any other work performed by the auditor or auditing firm.
5. Present proposals to the Board as regards the selection of auditors.

Other tasks undertaken by the Committee may be as follows, if appropriate:

1. Assessing financial statements and management reports on the company's finances.
2. Monitoring risk management and responses to risks.
3. Following-up on remedies to deficiencies that are discovered during internal controls.
4. Assessing the need for and handling the recruitment of an internal auditor.
5. Being responsible for communications and monitoring with respect to internal auditing and the auditors.

Detailed provisions on the execution of the roles of the Audit Committee must be included in its rules of procedure.

## B.1 Remuneration Committee

The Board may appoint a Remuneration Committee to establish a remuneration policy for the company and to negotiate with the CEO and other employees, who are also Director of the Board, as regards wages and other employment terms.[4]

The operation of a Remuneration Committee is particularly recommended in cases where the CEO is also a Director of the Board or where the Chairman or other Directors are also employees of the company.

## B.2 Appointment of Committee Members

The Remuneration Committee must consist of at least three members, the majority of whom must be independent of the company and its day-to-day management. However, the Committee may consist of two members, in which case both members must be independent of the company.

Due to the nature of the activities of the Remuneration Committee, neither the CEO nor other employees may be a member of the Committee. If the Board finds it more suitable to undertake the role of the Remuneration Committee itself, the Directors of the Board who are also employees of the company may not be involved in such work.

Committee members should preferably have experience and knowledge of the criteria and customs that relate to the determination of the employment terms of managers and be able to perceive the maximum payments to individual managers, e.g. on termination of employment, and their effects on the company.

## B.3 Role of the Remuneration Committee

The Remuneration Committee shall undertake the role of the Board to prepare and execute proposals for the employment terms of Board Directors and negotiate with day-to-day managers.

The role and main tasks of the Remuneration Committee must be stated in its rules of procedure and must take account of the needs of the company.

The role of the Committee should include, e.g.:

- Preparing the company's remuneration policy.
- Ensuring that wages and other employment terms are in accordance with laws, regulations and best practices as current from time to time.
- Negotiating with the CEO as regards wages and other employment terms, within the framework of the company's remuneration policy.
- Negotiating with other employees who are moreover Directors of the Board as regards wages and other employment terms, within the framework of the company's remuneration policy.
- Negotiating with the CEO and Directors of the Board as regards their retirement.
- Taking an independent stance as regards the effects of wages on the company's risk exposure and risk management.

The Remuneration Committee may seek the involvement of consultants in the execution of its duties. Such consultants must be independent of the company, its day-to-day managers and those Directors of the Board who are not independent. The Committee is responsible for verifying that such consultants are independent.

## B.4 Remuneration Policy

The Remuneration Committee must prepare the company's remuneration policy as regards the wages and other employment terms of the CEO, day-to-day managers and Directors and submit it to the Board for approval. If a Remuneration Committee has not been established, the Board must undertake this role.[5]

The Board must publish the company's remuneration policy in connection with its AGM, e.g. on its website, and the remuneration policy must be approved at the AGM, with or without amendments. At the AGM, moreover, the terms pertaining to individual managers and Directors of the company must be made known, including wages, earned pension payments, other payments and benefits, as well as any changes to terms between years.

Furthermore, information must be provided on the estimated cost of option plans and on the execution of the previously approved remuneration policy. This must be done to enable shareholders to fully understand the material arrangements of the employment terms of Board Directors and the CEO. If the Board departs from the remuneration policy, such departure must be submitted to the Remuneration Committee for approval, if such Committee has been established. Reasoning for such departure must be entered in the minutes of the Board in each case.

The remuneration policy[6] must state the basic aspects concerning the employment terms of managers and Directors and the company's policy concerning agreements with managers and Board Directors. It must also state whether, under what circumstances and within which framework it is be permissible to pay or reward managers and Directors in excess of basic wages, e.g. in the form of:

1. The delivery of shares.
2. Performance-linked payments.
3. Share certificates, purchase and selling rights, pre-emptive rights and other forms of payment which are linked to share certificates in the company or the development of the price of shares in the company.[7]
4. Loan agreements (thereunder special credit terms), provided that these are permitted by law.
5. Pension agreements.
6. Retirement agreements.

In the event of plans to reach agreements with managers and other employees for option rights to shares, or if such individuals are sold shares carrying selling rights, the main provisions of such contracts and/or plans must be submitted to a shareholders' meeting for approval. Main provisions include e.g. the total number of shares in the plan, the maximum length of option agreements, the period in which employees can exercise such rights, criteria for the determination of the purchase price and terms, in the event of a loan.

If the option plan also applies to Directors of the Board, it is recommended that this part of the option plan be discussed at a shareholders' meeting concurrent to discussion on remuneration to Directors.

## B.5 Basic Aspects of the Remuneration Policy

The company's remuneration policy should be based on a number of basic features, all of which have the common goal of ensuring that the interests of Board Directors and managers are actually connected with the long term success of the company.

To prevent the employment terms of the managers of the company from having the effect of encouraging excessive risk taking which provide short-term benefits rather than focusing on its long-term results, it is recommended that the remuneration policy take account of the following basic aspects:

1. On determining the employment terms of managers, account should not only be taken of the employment terms of their peers in other companies, but also of the employment terms of other employees of the company in order to ensure a harmonised and fair remuneration policy within the company.
2. Variable wages should be a normal proportion of overall wages. The remuneration policy should provide for maximum variable wages.
3. Variable wages should be linked to goals that reflect the company's actual growth and actual financial benefits in the long term for the company and its shareholders. These goals should be reviewed by independent Directors of the Board or the Remuneration Committee.
4. Variable wages should take account of the overall results of the company, long-term profitability, risk factors and financing costs. They should, moreover, be in accordance with risk management and reflect the effects of the profits of individual units on the total value of related units and the company as a whole.
5. It is recommended that the greater part of variable wages, such as annual bonuses, be paid after the company has shown good results for some time, e.g. 2 – 4 years.
6. The settlement of stock option agreements should generally not take place unless performance-linked goals have been reached and where pay-out is possible in tune with the time that the risk relating to such goals remains. A proportion of the settlement relating to stock option agreements with Directors who are not independent should not take place until after the Directors have retired from the Board. With the exception, however, of the proportion that must be sold to meet tax obligations that have formed as a result.

7. Stock option agreements which are not based on performance-linked goals should generally not be a part of the company's remuneration policy. Stock option agreements and their settlement should take account of the listed rate of the shares as current from time to time.

8. The remuneration policy should include a reservation to the effect that it is possible to demand the repayment of paid-out performance-linked payments if it is discovered after payment that performance goals were achieved by wrongful means or abuse.

9. Severance payments should be limited to the payment of wages for two years from the notification of termination, irrespective of its entry into effect, and should not be paid if the termination can be traced to poor performance.

10. Information should be provided on earned pension rights. Increases in such rights which are not pre-determined and which do not fall under the company's remuneration policy should be avoided.

11. The Remuneration Committee or independent Board Directors should have authorisation to change the criteria on which the employment terms of other Directors and managers are based in order to ensure that their overall employment terms are fair in light of the company's performance and their own performance and to ensure that they are not excessive.

12. The methodology, principal rules and goals of variable wages must be transparent to the company's shareholders and other stakeholders.

## C.1 Nomination Committee

The Board may decide to establish a Nomination Committee to improve efficiency and transparency in matters pertaining to the nomination of Board Directors.

By means of the establishment of the Nomination Committee, clear arrangements are made for the nomination of the Board of Directors at the company's AGM which, among other things, creates the foundation for informed decision making for its shareholders. In addition, it increases the likelihood that the company's Board will include diversity and breadth in capabilities, experience and knowledge. This is because the Committee is specifically expected to take account of these aspects when preparing nominations of Directors.

## C.2 Appointment of Committee Members

The Nomination Committee must consist of at least three members, the majority of whom must be independent of the company and its day-to-day management. However, the Committee may consist of two members, in which case both members must be independent of the company.

Due to the nature of the Committee's work, neither the CEO nor another employee who is considered to be a day-to-day manager of the company may be a member of the Committee. In addition, at least one member of the Committee must be independent of the company's major shareholders. The Directors may take a seat in the Committee but may not, however, form its majority. The Chairman of the Board may not be the Committee's chairman.

The Nomination Committee must be established no later than six months prior to the AGM. The Board is responsible for the establishment of the Committee. The appointment of the Committee must be posted on the company's website, and the arrangement of the appointment must be stated in its governance statement. If any Committee member represents a particular shareholder, the name of the shareholder in question must be specified. The company's website, moreover, must contain information on the manner in which shareholders can submit proposals for Board appointments to the Committee. The Committee should preferably request proposals from shareholders at least two weeks before the AGM.

During the company's AGM, the Committee should preferably inform the meeting of the manner in which it arranged its work and, moreover, explain its proposals.

## C.3 Role of the Nomination Committee

The Nomination Committee must nominate candidates for membership on the company's Board before its AGM.

On the execution of its work, the Committee must take account of the overall interests of the shareholders. The role and main tasks of the Committee must be stated in its written rules of procedure and must take account of the needs of the company.

The role of the Committee[8] should include, e.g.:

- Preparing and submitting proposals, based on the below assessment, on the election of Board Directors during the company's AGM.
- Assessing prospective Directors based on qualifications, experience and knowledge.
- Evaluating the independence of Directors.
- Addressing gender ratios on the company's Board.
- Informing prospective Directors of the responsibilities involved in Board membership in the company.
- Ensuring that shareholders receive information on Board Directors.
- Processing the results of the annual effectiveness assessment of the Board and executive management.

The Committee's proposals must be presented in the notice of the AGM and must be accessible to shareholders on the website of the company as soon as possible and at least five working days before the meeting. In the event of candidatures for the Board after the Committee's proposals have been posted and within two working days before the AGM, the Board of the company must disclose such candidatures on the company's website. Moreover, the company's website must contain the principal information on prospective Board Directors and the Committee's reasoning for its proposals together with its evaluation of the independence of the prospective Directors.

The Nomination Committee may seek the involvement of consultants in the execution of its duties. Such consultants must be independent of the company, its day-to-day managers and those Directors of the Board who are not independent. The Committee is responsible for verifying that such consultants are independent.

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[1] According to Art. 2 of the Act on Annual Accounts, an Audit Committee must be established in public-interest entities.

[2] In companies, other than public-interest entities, the Committee may consist of two persons, in which case both must be independent of the company.

[3] Cf. Article 2(b) of the Act on Annual Accounts.

[4] According to Article 79.a of the PUBLC Act, the Boards of companies under obligation to appoint an auditor pursuant to the Act on Annual Accounts must approve the company's remuneration policy.

[5] Cf. paragraphs 2 and 3 of Article 79 of the PUBLC Act.

[6] Cf. paragraph 1 of Article 79 of PUBLC Act.

[7] The remuneration policy is binding for the Board as regards these payments, cf. paragraph 2 of Article 79 of the PUBLC Act.

[8] As regards the role of the Committee and its proposals, see further guidelines no. 2.4, 2.5, 2.6 and 1.2.

# 6. Information on Corporate Governance

## 6.1 Corporate Governance Statement

A statement on the company's governance must be published annually in a separate chapter in its annual accounts. The annual accounts must be accessible on the company's website.

The statement[1] must contain the following items:

1. References to the rules on corporate governance that the company follows or is obliged to follow pursuant to law and where such rules can be accessed by the public.
2. Whether the company departs from the rules or applies none of their provisions. The reason for departure must be stated, as must the measures used instead.
3. A description of the main aspects of internal controls and the company's risk management in connection with the preparation of financial statements.
4. The company's values, code of ethics and social responsibility policy.
5. Description of the composition and activities of the Board, management and sub-committees of the Board.
6. Arrangement of the appointment of sub-committee members.
7. Information on the number of Board meetings and sub-committee meetings as well as their attendance.
8. Where written rules of procedure for the Board and its sub-committees may be accessed.
9. Information on Board Directors.
10. Information on which Directors are independent of the company and major shareholders.
11. Principal aspects in the Board's performance assessment.
12. Information on the company's CEO and a description of his main duties.
13. Information on violations of laws and regulations that the appropriate supervisory or ruling body has determined.
14. Arrangement of communications between shareholders and the Board.

The above applies equally to the consolidated financial statements.

In addition, it is recommended that the Board forms an opinion on whether the company's corporate governance statement contains an analysis of environmental factors and social factors that are necessary to understand the development, success and position of the company, such as the manner in which the company bears social responsibility.

The Audit Committee must review the company's corporate governance statement, and the company's auditor must ensure that it is included in the annual accounts and that its description of the main features of internal controls and risk management is in accordance with the company's financial statements.

## 6.2 The Company´s Website

The company must reserve a section of its website for good corporate governance and must publish its corporate governance statement there as well as other data.

To increase transparency in the operation of the company, it is important that all principal information on its activities is available on its website.

The company's website should among other things contain the following information:

1. The company's corporate governance statement.
2. The company's remuneration policy.
3. Summarised information on the company's Board of Directors, CEO, auditors and members of committees.
4. Information on the company's shareholders' meetings, including time and location, information on candidates to the Board and the agenda of the meeting together with the date of issue of the annual accounts and interim financial statements.
5. The company's annual accounts and the report of the Board of directors.
6. The minutes of shareholders' meetings.

It is recommended that the above information is updated within 7 days from the time that the Directors and/or the executive managers become aware that the information has changed.

[1] With regards to the content of the company´s govervence statement see further guidelines no. 2.4, 2.5, 2,6, 2.9, 2.11 og 4.1.

# Appendices

## I. Related Rules and Regulations

May acts and regulations within the Icelandic regulatory framework contain provisions on corporate governance, both directly and indirectly. In addition, the management of companies requires attending to various types of decisions made by public officials.

Below is a short summary of such regulatory provisions as well as others that concern corporate operations in general:

- Rules for issuers of financial instruments on NASDAQ OMX Iceland hf.
- Act on Activities of Stock Exchange No. 110/2007.
- Act on Electronic Registration of Title to Securities No. 131/1997.
- Act on Public Limited Companies No. 2/1995.
- Act on Private Limited Companies No. 138/2004.
- Act on Partnerships No. 50/2007.
- Competition Act No. 44/2005.
- Act on Auditors No. 79/2008.
- Act on Annual Accounts No. 3/2006.
- Act on Securities Trading No. 108/2007.
- Act on Measures Against Money Laundering No. 64/2006.
- Act on Public Supervision of Financial Activities No. 87/1998.
- Act on Mandatory Insurance of Pension Rights No. 129/1997.
- Act on Undertakings for Collective Investment in Transferable Securities and Investment Funds No. 30/2003.
- Act on Insurance Operations No. 60/1994.
- Act on Financial Undertakings No. 161/2002.
- Act on Supervision of Business Practices and Marketing No. 57/2005.
- Act on Consumer Goods Purchases No. 48/2003.
- Act on Foreign Currency No. 87/1992.
- Act on the Equal Position and Equal Rights of Women and Men No. 10/2008.
- Act on Contracts, Agency and the Invalidation of Legal Instruments No. 7/1936.
- Act on Hygiene and Pollution Prevention No. 7/1998.
- Act on Working Environment, Health and Safety No. 46/1980.
- Act on the Protection of Privacy as Regards the Processing of Personal Data No. 77/2000.
- Recommendations and interpretations of the Financial Supervisory Authority (see www.fme.is).
- Decisions of the Financial Supervisory Authority (see www.samkeppni.is).

# II. Models

Although the guidelines are based on the Icelandic regulatory framework and reflect Icelandic conditions, they nevertheless take account of international developments in this field. The main models used as guidance in the preparation of these guidelines were:

- Business Roundtable: Guidelines for Shareholder-Director Communications (2005) og Principles of Executive Compensation (2007).
- Corporate Governance in the Nordic Countries (2009).
- The European Corporate Governance Forum: Executive remuneration (IP/09/459 - 2009).
- Financial Reporting Council: Review of the effectiveness of the Combined Code on Corporate Governance (2009).
- Financial Reporting Council: The Combined Code on Corporate Governance (2008).
- Finnish Corporate Governance Code (2008).
- Higgs Suggestions for Good Practice – UK Code of Best Practice (2003).
- KPMG: Integrity Survey 2008-2009.
- NYSE Corporate Governance Rules (2003).
- OECD Principles of Corporate Governance (2004).
- OECD: The Corporate Governance Lessons from the Financial Crisis (2009).
- PriceWaterhouseCoopers: Endurskoðunarnefnd (2008).
- PriceWaterhouseCoopers: Innra eftirlit (2008).
- Report on Banking Regulation and Supervision in Iceland: past, present and future (2009).
- The Belgian Code on Corporate Governance (2009).
- The Danish Committee on Corporate Governance Recommendatoins for corporate governance (2008).
- The Danish Government – Action plan for corporate social responsibility (2008).
- The European Corporate Governance Forum: Director Remuneration (2009).
- The Norwegian Code of Practice for Corporate Governance (2007).
- The Swedish Code of Corporate Governance (2008).
- The Turner Review: A regulatory response to the global banking crisis (2009).
- UN Global Compact – 10 principles for social responsibility.

## III. What is Corporate Governance?

As corporate governance takes, for the most part, account of the circumstances, traditions and customs in the country in question, no internationally approved definition of the term has been created. The term, therefore, has been used as a synonym for basic factors in management. In Iceland, the definition commonly used is that corporate governance relates to the tripartite relationship between shareholders, the board of directors and the executive directors. On a wider note, the term also covers the relationship between the company and other entities on which the operation of the company has an effect, such as employees, creditors and the community.

By describing this extensive relationship, one could say that the purpose of guidelines such as these is to harmonise conduct criteria within companies as regards these basic factors in their management. They are, therefore, generally considered as a response to market entity expectations for foreseeable patterns of behaviour in all parties within the company – and in fact the economic sector as a whole – in excess of what legislation provides for. The guidelines thus continue on from where legislation leaves off and involve increased obligations for the management of companies in various fields. They are, therefore, not intended to replace the official legislative framework, but rather they are based on the legislative framework, business practices and international guidelines that have analysed several common characteristics of good corporate governance.

By following these guidelines, and voluntarily undertaking increased obligations, company managers are laying the foundations for trust as regards the company's activities. Follow-ups on guidelines of this nature are, moreover, generally considered to assist management in reducing risk and increasing economic benefits for the company and its shareholders in the long term. With follow-ups, companies maintain their competitiveness and adapt the arrangement of corporate governance in such a manner that they can meet new demands and take advantage of new opportunities.

The goals of the guidelines are e.g. to:

- Encourage good corporate governance in Iceland.
- Make it easier for board members and managers of companies to meet their obligations and thus make it easier for them to promote the growth and prosperity of the companies they are entrusted with.
- Increase trust in companies and business operations in general.
- Strengthen trust between investors and managers.
- Increase the competitive capabilities of the Icelandic business sector by making sure that Icelandic corporate governance is largely the same as in our neighbouring countries.
- Make it easier for investors to understand the corporate governance methods generally used in Iceland when they assess their investment options.
- Facilitate access to credit in Iceland and overseas for Icelandic companies.

To achieve these goals, the guidelines are intended to describe the separations, relationships and responsibilities between the management of the company, board members, shareholders and other stakeholders, particularly those involving differences of opinion resulting from the separation of management and ownership. Moreover, they are expected to establish a structure for the goals of the company, means to achieve such goals and policies on the manner in which controls are arranged. This structure, moreover, is an appropriate incentive for the board and management to follow goals that are beneficial to the company, its shareholders and its operating environment.

Guidelines of this nature also assist the authorities in establishing a regulatory framework in this field. It is difficult for the authorities to address a large number of disputes relating to the corporate governance of different types of companies in legislation. They generally, therefore, have to craft general rules that apply to all companies. In addition, amending existing legislation is very often time-consuming. Guidelines of this nature can, therefore, support general legislation and ensure that corporate governance in the Icelandic economic sector can adapt quickly in accordance with best practices internationally. Active co-operation between the authorities and the economic sector means that it is possible to utilise the advantages of regulations and guidelines to establish credible corporate governance in Iceland.

## VI. The "Comply or Explain" Rule

The comply or explain rule is one of the basic features in guidelines on corporate governance. The rule grants the managers of dissimilar companies scope to adapt the guidelines to the extent appropriate to their type of operations and operating environment.

Increased scope, however, requires more detailed provision of information in areas where the guidelines are not followed. Generally worded explanations of deviations do not suffice; instead sound reasoning must be given for the deviation. Furthermore, information must be provided as to whether any other measures have been taken and, in such case, what measures have been taken. In this manner, shareholders are given the opportunity to assess whether such measures better ensure that the board operates on behalf of their long-term interests. In addition, it is clear that without such provision of information, the goal of the guidelines for increased transparency and thereby increased credibility could not be reached.

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