

## Första AP-fonden's Ownership Policy

Effective from 13 December 2016

### Introduction

Första AP-fonden is a long-term investor and an engaged owner. This means amongst other things that the Fund has high ambitions for Corporate Governance, as well as for sustainable value creation.

Första AP-fonden's actions with regard to ownership issues are based on a business-oriented approach and knowledge about the individual company, and are always steered by what is best for the companies and their shareowners over time, and therefore also for those insured in the pension system. In its actions, the Fund shall also seek to benefit the company in question and promote an efficiently functioning capital market. By being business-oriented and transparent, taking a long-term approach and with high integrity in its action, the Fund builds trust in companies, other owners and stakeholders, and among the general public.

The Fund presumes that the businesses it invests in adhere to international conventions, the Global Compact and the national legislation of the countries where they operate. It is the responsibility of the board to ensure that there are adequate processes and controls to secure this.

Corporate law, traditions and codes of relevance for corporate governance that apply in the market where the company is based are also important and can also affect the Fund's position in individual cases. In addition to laws, traditions, corporate law and codes, the Fund's position is based on eight principles for corporate governance and the companies' social and environmental responsibility. Each principle is divided into two parts, of which the first contains general principles that apply to all companies where the Fund has holdings, regardless of their nationality, and the second applies only to Swedish companies. Första AP-fonden has formulated special rules for Swedish companies because the Fund generally has larger holdings in these companies, and therefore also greater opportunity to influence them. The Ownership Policy applies to shares that are managed both in-house and by external managers and to both listed and unlisted shares, although the Fund has significantly smaller scope to influence unlisted companies that are owned indirectly. However, it is vital that the requirements for listed companies do not become so onerous that companies avoid listing on a marketplace.

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For companies in which Första AP-fonden has significant voting power (associated companies<sup>1</sup>), special owner directives should be adopted. The companies should be good role models in Corporate Governance issues. Aside from the eight principles below, remuneration to senior executives in the company should comply with “The Swedish Government’s guidelines for remuneration to senior executives in government enterprises” (2009-04-09). Any deviations from these guidelines must be motivated. In associated companies, Första AP-fonden should have its own representation on the company’s board of directors.

Greater results can be achieved by coordinating the Fund’s actions in shareowner issues with those of other shareowners. Första AP-fonden therefore seeks to cooperate with other shareowners – both Swedish and foreign – where appropriate and in accordance with the Fund’s Ownership Policy. The failure of other shareowners to act does not constitute reason for the Fund to refrain from taking measures of its own.

Första AP-fonden uses a three-step process to handle any conflicts of interest. The first step is to identify possible conflicts of interest in advance. The second step is to handle any conflicts of interest through the Managing Director’s decision regarding the Fund’s action in each individual case. For conflicts of interest of particular significance, the Board Chairman is also consulted. Existing conflicts of interest are reported to the board and published on the Fund’s website as they arise.

Active external communication conveys a clear profile that strengthens the Fund’s credibility. The Fund’s views on individual companies are primarily discussed directly with the company’s board and management group. If the discussion has no successful outcome, the Fund will consider expressing the views publicly. Ultimately, the Fund may consider selling the holding.

## **Eight principles for Corporate Governance**

### **1. Voting rights and right of proposal at general meetings**

*The general meeting of shareowners is the company’s highest decision-making body, and the exercise of voting rights at general meetings is an important tool for shareowners to exert their ownership influence. Första AP-fonden works to ensure that this right is unrestricted. This also means that the shareowners must be able to propose items for the agenda of general meetings, and be entitled to have these matters discussed.*

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<sup>1</sup> In most cases, a voting share of more than 10 percent. According to the Swedish National Pension Funds Act, this is permitted only for real estate companies.

## 2. Equal treatment

*Första AP-fonden's position is that shares granting equal financial rights in a company should always be treated equally in a financial respect. Deviations from this principle are permitted only as specifically stated in a company's articles of association. It is important that the interests of minority shareowners are protected.*

**For Swedish listed companies:** In the Swedish market it is common for companies to have classes of shares with differentiated voting rights (class A and B shares) but with equal financial rights to the company's assets and profits. In order to maintain confidence in this system, it is essential that the equal treatment principle is upheld. For Första AP-fonden it is important that no shareowner is discriminated against financially in connection with (i) payment of dividends – regardless of whether payment is made in cash, shares in subsidiaries or some other manner, (ii) liquidation of a company, or (iii) bids for all shares in a company.

## 3. Capital structure

*Companies should seek a capital structure that is appropriate with regard to the company's future opportunities to generate returns for its shareowners. Capital that cannot be effectively used to safeguard or develop the company's operations in accordance with its strategy should be distributed to the shareowners. The Fund's position is that the shareowners should have opportunities to vote at general meetings regarding new share issues, dividends and buy-backs of the company's own shares. Directed buy-backs should not be carried out at prices exceeding the current market price at any given time.*

*As a rule, new share issues should be resolved on by the general meeting of shareowners and should be carried out as cash issues with pre-emptive rights for the company's existing shareowners. Only in specific situations is it justifiable to deviate from the pre-emptive rights of existing shareowners (preferential issues). Shares issued on a preferential basis shall not be priced at discount. Authorization for the board to carry out issues may be necessary but should not exceed 10% of the company's share capital and should not extend longer than until the next annual general meeting. In the event of non-cash issues, a thorough and detailed evaluation should be published to enable the shareowners to assess the terms of the issue in relation to the acquired assets.*

*All deviations from the normal case, a pre-emptive rights issue resolved on by the general meeting, must be motivated in detail by the company's board of directors. Första AP-fonden will then make a restrictive assessment of the board's motives.*

*It is not in the best interests of the shareowners for a company to set up any type of obstacle to acquisition of the company. Första AP-fonden is against the implementation of such obstacles and is in favour of eliminating them.*

**For Swedish listed companies:** A transparent and clear system of voting rights differentiation should not be prohibited by law. The Swedish system of class A and class B shares is more transparent than many other systems. Respect for ownership rights demands that any changes in voting rights be carried out voluntarily. In certain cases, however, the disadvantages of having different share classes outweigh the advantages. In such cases, Första AP-fonden will take action to promote a change in the differentiation of voting rights.

As the preferred alternative, Första AP-fonden advocates the use of general methods such as pre-emptive rights issues, extra dividends and redemption programmes to adjust the capital structure. A buy-back of the company's own shares may therefore be used when no other means are appropriate. Share buy-backs should be undertaken only for the least expensive share class at any given time, if the company has more than one class of shares. It may be cost-effective to use a share buy-back as part of a hedge of the company's share-based incentive schemes. Shares that are repurchased for other reasons should be cancelled and the sale of such shares should not be permitted. Proposals for a buy-back of the company's own shares must be well motivated.

## 4. The companies' boards of directors

### Election of board members

*The right to nominate and vote for board members at a general meeting is of fundamental importance for the shareowners. Första AP-fonden's position is that nomination of the chairman and board members should take place through a clear and open nomination procedure. Första AP-fonden also works to prevent restriction of shareowner influence on election of board members and – if possible – to increase it.*

**For Swedish listed companies:** The process of appointing board members has been systematized and, thereby, considerably improved since the general meetings of shareowners started to elect nomination committees. It should be emphasized that the nomination committee is not a corporate body but works on behalf of the general meeting of shareowners. The nomination committee should not evolve into a body whose task is to oversee the work of the board. Första AP-fonden actively participates in the nomination of board members and, as a rule, takes part in the nomination committees of the companies where this is warranted by the size of the Fund's shareholding. Otherwise, the Fund cooperates with the sitting nomination committee in cases where the Fund feels that a change in the composition of the board would benefit the company and its shareowners.

The nomination committee has an extensive need for information from the board of directors – primarily, but not solely, via the chairman – about the board's performance and competency requirements.

Första AP-fonden's position is that the chairman should preferably be co-opted to the nomination committee, but the chairman can also be a regular member of the committee. In the latter case there is sometimes reason to exclude the chairman from certain deliberations and decisions. The nomination committee should receive information from other board members by meeting with the board either individually or as a group. Members of nomination committees must be prepared, in exceptional cases, to receive and handle insider information. Första AP-fonden's strives to ensure that no more than one board member (including the chairman) should be a member of the nomination committee. If more than one board member is on the nomination committee, this must be well motivated.

## Composition of the board

*Expertise and integrity are important attributes for a board member. Effective board performance requires diversity in the composition of the board to achieve the necessary breadth in the members' combined experience and knowledge. Första AP-fonden therefore strives to widen the recruitment base for board candidates and thereby achieve a more even gender distribution and an increased share of ethnic minorities.*

*Första AP-fonden's position is that a company's board chairman and managing director should not be one and the same person. Each board of directors should include members who have an independent status in relation to the company's management and major shareowners. The board's remuneration, nomination and audit committees should be fully independent from the company. Första AP-fonden is in favour of electing the board for one year at a time.*

**For Swedish listed companies:** The boards of directors should be made up of members with the requisite competence and experience, high integrity, good availability and strong commitment. The board members should devote the amount of time and attention needed to carry out their work in a satisfactory manner, always with the interests of all shareowners in view.

The composition of the board should be continuously adapted to the respective company's business operations, external conditions, market and phase of development. The board of directors should consist of members with diverse competencies, backgrounds and perspectives. Första AP-fonden strives for an even distribution between men and women on the boards. The boards should also have a balanced mix of individuals with different backgrounds and perspectives, e.g. in terms of age, nationality and ethnic origin. The company's managing director may be a member of the board.

## Remuneration to board members

*Remuneration to the chairman and other members of the board should be market-based and should reflect the demands placed upon them. Första AP-fonden is in favour of board members owning shares in the company, but does not feel that this need be a mandatory requirement.*

**For Swedish listed companies:** Första AP-fonden's position is that directors' fees should be determined in a fixed amount. However, this does not prevent payment of part of the fee in the form of actual or synthetic shares. Första AP-fonden also advocates systems that are designed so that the shares are not freely transferable until after an extended period of time (lock-up period).

## 5. Remuneration to senior executives and incentive schemes

*Första AP-fonden's position is that management remuneration should be structured in such a way that it benefits the company and its shareowners. Such remuneration encourages the employee to act in a way that increases the company's long-term profits at the same time that a suitable level of risk is maintained in operations. The remuneration system may not serve as an incentive for illegal or otherwise inappropriate actions. Första AP-fonden promotes remuneration that is reasonable, market-based and consistent with best practice in the local*

*market, and should be moderate enough that it can be clearly and openly motivated to the company's stakeholders. The remuneration system should not undermine the confidence of the company's stakeholders. Information about the structure of compensatory programmes should be detailed and accurate, regardless of whether these are resolved on by the general meeting or not.*

**For Swedish listed companies:** Responsibility for determining the level of remuneration to the managing director lies with the company's entire board, regardless of whether this has been resolved on by the general meeting or not. The total amount of remuneration should be reasonable and market-based. The remuneration system and process for determining the amount of remuneration to the managing director and senior executives should be characterized by openness and should not undermine the confidence of the companies' stakeholders. In the event that remuneration to senior executives leads to share ownership, the company should promote ownership of the shares for an extended period of time, in most cases even for some time after employment has ended.

### **Fixed remuneration**

A certain proportion of the fixed remuneration may be paid in the form of shares in the executive's own company. The principles for remuneration to senior executives should contain information about how this proportion is determined.

### **Variable cash remuneration**

Any variable cash portion of remuneration should be performance-related, evaluable and in most cases linked to the company's profitability. Första AP-fonden's position is that a large proportion of the performance targets should be set in relation to the company's competitors. It is important that the variable remuneration does not serve as an incentive for short-term actions or undesirable risk taking.

Första AP-fonden is of the view that it is, in many cases, an advantage if short-term variable remuneration is small in relation to long-term variable remuneration.

### **Long-term share-based incentive schemes**

Aside from fixed and variable remuneration, there are long-term share-related incentive schemes where the goal is to ensure that the interests of senior executives are aligned with those of the shareowners. Such schemes also provide the opportunity to offer a market-based total remuneration comparable to that offered in many other countries.

Whether or not a long-term incentive scheme is market-based must be judged in relation to the other parts of the remuneration package. It is important to thoroughly analyze the scheme and gain the support of the shareowners before a decision is made at the general meeting. The incentive scheme should be part of a communicated long-term remuneration strategy.

### **Schemes with own investment**

A market-based payment in order to participate in an incentive scheme is equated with a performance requirement. Första AP-fonden therefore approves incentive schemes that require a market-based price for participation. Första AP-fonden considers it favourable if employees own shares in the company. To encourage this the company may, under certain conditions and at a reasonable cost, subsidize programmes aimed at increasing share ownership.

### **Schemes without own market-based investment**

In order for a long-term share-based incentive scheme to have the intended effect, Första AP-fonden's position is that the following criteria must be met:

- The achievement of pre-determined, clear and measurable targets shall be required in order to qualify for allocation in share-related incentive schemes. As a rule, the performance targets should be linked to the company's long-term value creation. Incentive schemes should not reward the participants for the event of a general stock market rally. If the programmes are related to the company's share price performance, they should preferably be relative, i.e. the company's share price performance is related to development across the entire stock market, share price performance in the industry or share price performance for selected competitors. The targets should be set in a way that does not encourage unwanted risk-taking or other undesirable behaviour.
- The criteria for the performance targets shall be communicated to the shareowners prior to a decision by the general meeting, although it is acceptable not to provide information about the levels for goal attainment. Information about the level of goal attainment required for a particular award shall be provided when the term of the scheme has ended.
- Long-term share-related incentive schemes expose the company to a risk for movements in the price of its own shares. Information about how the company intends to manage this risk, and the related costs, shall be put before the general meeting prior to a decision.
- There should be an upper limit in the value of the scheme, particularly if it is not relative.
- The costs for and effects of previously implemented schemes should be regularly evaluated as a basis for decisions on future schemes. The evaluation should be carried out from a shareowner perspective and should be presented to the shareowners before a decision is made on new or continued incentive schemes. The board is responsible for performing the evaluation and for ensuring that the shareowners are provided with clear and straightforward information about the results. If a satisfactory evaluation is not presented prior to the proposal of an incentive scheme, Första AP-fonden will vote against the scheme.

## Pensions

Pension provisions for senior executives are part of the total remuneration package and must therefore be judged in relation to other types of remuneration. Pension benefits and the companies' current and anticipated future pension expenses must be reported in detail. Första AP-fonden's position is that the pension plans of senior executives should be of the defined contribution type. However, existing contracts should be renegotiated only when motivated from a cost perspective.

## 6. Audit and internal control

*It is in the interests of the shareowners that a company's external audit and internal control are of adequate quality. Very strict requirements should be made regarding the independence of external auditors from the company and its management.*

**For Swedish listed companies:** Auditors are appointed by the company's shareowners and have the role of independent examiners. Första AP-fonden stresses the importance of having competent auditors with sufficient resources to conduct an audit of high quality. The auditors should provide detailed information about company audits to the shareowners, both in the audit report and at the general meeting.

The effectiveness of a company's internal control is of the utmost importance in building confidence in the company and the stock market in general. Första AP-fonden places high demands on the completeness and accuracy of a company's description of internal control in the corporate governance report. Any explanations about the rules in the Swedish Code of Corporate Governance regarding internal control are studied carefully.

## 7. Environmental and social issues

This principle applies to both Swedish and foreign companies.

Operations should be conducted in a financially, environmentally and socially responsible manner. Första AP-fonden's view is that the companies themselves are responsible for compliance with international conventions, regardless of whether these are directed to national governments, to individuals, or to companies and organizations. Moreover, this responsibility applies regardless of whether the countries in which these companies operate have signed the conventions or have weaker legislation. Första AP-fonden expects all of the companies it invests in to live up to the ten principles for corporate responsibility that are defined in the UN's Global Compact, and to include sustainability issues in formulating the company's business strategy.

The AP1, AP2, AP3, and AP4 work through the joint Ethical Council to monitor environmental and social compliance in the companies where the funds have holdings. Decisions regarding measures to be taken regarding the companies are made by the individual funds.

### **Första AP-fonden's basic principles**

As part of the Swedish pension system, Första AP-fonden bases its principles on the core values applied by the Swedish government, where democracy and sustainable development are central components in accordance with the rights and freedoms defined in the Instrument of Government.

Första AP-fonden's principles are based on the international conventions that have been signed by Sweden, including conventions relating to the environment, human rights, labour rights, corruption and inhumane weapons. In cases where Sweden declares its support for a new convention or modification of an existing convention that has not yet been formally ratified, the Fund will act as if such ratification has already taken place. Första AP-fonden will regularly monitor how the ratification process for the new or modified convention is progressing. In the event that Sweden has not ratified the convention within a period of three years from the date on which Sweden has declared its support for the same, Första AP-fonden may review the basis for its guidelines regarding the issues covered by the new or modified convention.

Första AP-fonden's view is that the companies it has invested in are themselves responsible for compliance with international conventions, regardless of whether these are directed to national governments, to individuals, or to companies and organizations. Moreover, this responsibility applies also where the countries in which these companies operate have not signed the conventions or have weaker legislation.

Första AP-fonden's position is that all of the conventions that have been ratified by Sweden are of equal importance and should therefore be adhered to. This position is also supported by the UN Declaration of Human Rights, which points out that human rights are universal, indivisible, interdependent and interrelated, and cannot be ranked internally. Första AP-fonden refrains from making any such ranking.

By tying Första AP-fonden's requirements to international conventions and by cooperating with others towards the same purpose, the Fund can contribute to international efforts to ensure that action is taken against infringement of conventions in the global financial market. This also serves to give the conventions greater weight.

Första AP-fonden's work on sustainability and Corporate Governance aims to create and protect values for current and future Swedish pensioners. Första AP-fonden makes a difference by proactively striving for sustainable development, acting and imposing demands on transparency and positive changes. This enhances Första AP-fonden's ability to fulfil its mission.

### **Första AP-fonden's assessment and measures**

Första AP-fonden's assessment of the companies shall be based on an official examination in each individual case. The Fund's assessment shall consider the seriousness of the offence and how it has been judged by the relevant authority. In this respect, deliberate or repeated infringements will be judged more severely. Any action that the company has taken or intends to take with immediate effect in order to correct the problem will be taken into account. Första AP-fonden works to ensure that the companies have viable policies, explicit goals, resources and action plans for improvement measures, as well as open reporting of their environmental and social responsibility efforts.

If a company in which Första AP-fonden has invested can be associated with infringement of any of the conventions that Sweden has ratified or recently declared its support for, the Fund will attempt to influence the company to bring about a change in order to avoid future infringements. Where possible, the companies should also provide compensation for damages to the affected individuals and correct any negative impact on the environment.

If it becomes obvious that the company has no interest in making changes or if the implementation of changes does not take place with the desired speed, Första AP-fonden will exclude the company from its investment sphere. A decision of this type means that all of the Fund's holdings of securities issued by the company – regardless of whether they are managed internally or externally – shall be divested as soon as feasibly possible. If the Fund terminates its ownership, the problems in question will not disappear and the unacceptable conditions will continue. For that reason, exclusion of the company from the Fund's investment sphere is a last resort, to be taken only when the opportunities to make a difference are without hope of success.

## 8. Information disclosure

This principle applies to both Swedish and foreign companies.

Companies should seek an open and continuous dialogue with the shareowners. The companies' information should be accurate, clear, objective and trustworthy. The information provided by the companies should enable qualified assessment of the company's future development and the factors that create value for the shareowners. The companies should strive for clarity with regard to their established goals and the financial and strategic consequences of these goals.

The companies should publish an ethics policy or code of conduct and an anti-corruption policy. The companies should also be transparent in matters related to tax, for example by publishing a tax policy. In addition, the companies should transparently describe how the policies and guidelines are implemented, monitored and evaluated.

### **Decision-making procedure**

This Ownership Policy applies from 13 December 2016 and replaces the earlier policy. The board of directors is the body that establishes Första AP-fonden's Ownership Policy. Ownership-related issues are addressed by Första AP-fonden's Managing Director directly or according to his delegation to another executive in each individual case. In ownership issues of greater importance, the Board Chairman should be consulted and the matter should then be reported to the Board. Ownership issues of particular importance should be referred to the board by the Chairman. Furthermore, ownership issues that are found to be of a significant nature at the time of reporting should be subject to treatment by the Board. At least once a year, the Managing Director shall report to the board on compliance with the Ownership Policy.